

Response to OECD consultation on the Pillar Two Blueprint

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Insurance Europe welcomes the opportunity to contribute to the Public Consultation Document on the Report on the Pillar Two Blueprint. The insurance industry sees favourably the efforts to reach a political agreement by mid-2021 and the developments which go in that direction.

Before answering the questions of most importance to the insurance industry set in the Public Consultation Document, Insurance Europe would like to highlight the key messages that will be further expanded below.

Key messages

Implementation issues

- Insurance Europe acknowledges the policy objectives underlying many of the design features of the GloBE rules, but the provisions remain far-reaching and complex, presenting significant implementation issues for MNEs.

Consolidated revenue threshold

- The insurance industry supports a single consolidated revenue threshold of €750m for the purposes of applying the GloBE provisions.

Approach to blending

- The European insurers feel that global blending provides a more appropriate balance between the policy objectives of the GloBE provisions and the overall administrability of those provisions and continue to support global blending as the preferred alternative to jurisdictional blending.
- Insurance Europe acknowledges the OECD preference for a jurisdictional basis, but advocate using a global calculation as a safe harbour (eg at a higher rate than the GloBE minimum) to provide a welcome simplification and remove the costly compliance complexity for many groups operating predominantly in high-tax jurisdictions.

Economic substance carve-out for (re)insurance services

- Insurance Europe believes that the carve-out proposed in the Pillar Two Blueprint is only appropriate for labour-intensive and tangible asset-intensive businesses, and therefore is not relevant for the financial services industry, and particularly for (re)insurance services.
- (Re)insurance companies operate around the globe under the careful oversight of regulators, which require specific and quantifiable amounts of capital to be held in specific entities to ensure the protection of policyholders. The allocation of capital follows that allocation of risk. That is, there are objective measures of how much capital is required to operate in a given jurisdiction. Highly regulated financial services companies such as (re)insurance undertakings can decide where to pool risks most efficiently, but once the location of risk is determined it is difficult to move.
- The amount of regulatory capital should be included in the formulas for the purposes of computing the substance-based carve-out, in order to more accurately reflect the economic substance of financial service entities.

Effective Tax Rate (ETR)

- The proposed effective tax rate (ETR) does not take timing differences — a fundamental aspect for insurance businesses — into account appropriately.
- Timing differences most prominently occur in the case of insurance reserves (eg liabilities to pay future benefits to policyholders) as a result of differing valuation rules under local tax laws and IFRS. Since such reserves represent a large portion of the balance sheet liabilities and since they take decades to be taken off the books, the insurance industry may be impacted by the way ETR is calculated far more than other industries. A small accounting difference for reserves can create large discrepancies.

Subject to Tax Rule (STTR)

- The insurance industry is concerned by the inclusion of insurance and reinsurance premiums in the definition of covered payments under the STTR, as BEPS risk payments. This seems at odds with the purpose of the STTR, which should not be applicable to normal regulated business transactions. The industry urges the IF to exclude insurance and reinsurance premiums from the scope of the STTR, in so far as they meet the criteria of genuine insurance business as defined in the OECD Transfer Pricing Guidelines.
- In particular, the sentence "If the risk does not materialise, the insurance or reinsurance premium can generate a high return." in the Pillar Two Blueprint (see Paragraph 601) misses the whole point of insurance. If the risk does materialise, a loss far exceeding the initial premium payment can arise, ie the risk of the adverse event occurring has been assumed by the insurer.
- In addition to that, Insurance Europe also underlines that the STTR as currently designed would have several other issues such as:
 - The risk of substantial over-taxation.
 - The detrimental effects on economically driven business models and group structuring, as it would have undesirable economic effects on legitimate business models in the insurance sector, in light of the differentiation between captives and reinsurance entities of insurance MNE groups.
 - Not taking into consideration the existence of transfer pricing comparables for (re)insurance premiums to mitigate the risk of artificial BEPS resulting from (re)insurance transactions.
 - The potential increase in pricing that insurance policies would incur under STTR.
 - The resulting increase in the compliance burden to set up a worldwide system to monitor and administer the withholding taxes paid.

Dispute resolution and prevention

- The interaction between the various types of tax regulations that may apply to MNEs worldwide may result in conflict-of-law issues and litigation. Insurance Europe supports the inclusion of robust dispute prevention and resolution schemes, as well as reasonable timelines in order to allow settlement within timeframes that would not hinder business.

Insurance Europe acknowledges that the public consultation on Pillar Two addresses more the technical aspects focussing primarily on administration, implementation, calculation and simplification. Nevertheless, the industry wishes to make some general comments on the Pillar Two Blueprint.

General comments

Compliance complexity

- Due to the complex rules under Pillar Two, there will be an inevitable increase in the compliance burden for companies as well as tax authorities. To offset at least part of the additional compliance burden, the introduction of the rules should be accompanied by a cutting back of existing anti-abuse rules with similar policy objectives. The envisioned rules already secure an effective minimum taxation of the (global) income of companies that are in the scope of Pillar Two. Due to the applicable minimum taxation as well as the increased compliance burden, exempting these in-scope companies from comparable national anti-abuse rules should be considered. Otherwise, the simultaneous application of national anti-abuse rules and the GloBE rules may result in double taxation as well as unnecessary bureaucratic expenditure.

Definition of revenues

- The GloBE rules should deal with diverging revenue definitions under IFRS and national GAAPs. Differing treatment exists for certain insurance products. There should be a common definition for the purposes of the €750m revenue threshold that determines whether an MNE group is within the scope.
- Many long-term insurance products include an element of savings and investment assets. Under German GAAP, all such income is recognised as revenue, although it would not be under IFRS. A revenue threshold for inclusion in the regime of €750m could result in insurers being brought within scope as a result of German GAAP including policyholder-related items within revenue that would not be included in the equivalent IFRS revenue.
- It is for this reason that revenues of insurance companies under German GAAP tend to be relatively high (banks, on the other hand, do not show customer deposits as revenues). Metrics applied to insurance groups should therefore adequately reflect the specific nature of the business and exclude policyholder items.
- A similar issue arises where the income derives from the investment assets held for the policyholders, such as portfolio dividends and interest income. These income streams should not be regarded as revenues for the purposes of the €750m threshold.

Recognition of national accounting standards (paragraph 173 of the Pillar Two Blueprint)

- MNE with a consolidated group revenue threshold of at least €750m are in the scope of the GloBE-rules under Pillar Two. Chapter 3.3.3 determines which accounting standards are accepted for the purpose of calculating the group revenue threshold. The Blueprint explicitly mentions IFRS and the national GAAPs of Canada, Japan, China, India, Korea and the USA. Non-listed companies in many cases use other national GAAPs of their home country. If they exceed the €750m threshold, they are in the scope of Pillar Two.
- European insurers welcome the statement in the Blueprint that other national GAAPs should be accepted if the use of that standard would not result in material competitive distortions in the application of the GloBE rules (see Paragraph 173 of the Pillar Two Blueprint).
- In our view, the European accounting standards meet these criteria and should therefore be accepted. For reasons of legal certainty, the generally accepted accounting standards should be explicitly listed. Any additional compliance burden resulting from a factual obligation for businesses to provide consolidated financial statements under international accounting standards only for the purpose of determining the tax rate under Pillar Two should be avoided.

Recognition of an unused IIR-Tax-Credit (see paragraph 309 of the OECD Pillar Two Blueprint)

- Insurance Europe welcomes the discussion within the Inclusive Framework on whether an unused IIR tax credit should be creditable against national corporate income tax. If the IIR tax credit can only be

used for the GloBE rules there would likely be cases where the tax credit expires lacking a top-up tax under Pillar Two in succeeding years. The situation can follow a raise of the tax rate in a formerly low taxing jurisdiction.

Premium Tax as Covered Taxes

- Section 3 of the Pillar Two Blueprint generally defines covered taxes as any tax on an entity's income or profits (including a tax on distributed profits), including taxes imposed in lieu of a generally applicable income tax. The industry appreciates the acknowledgement in Paragraph 139 that taxes on categories of gross payments such as insurance premiums should be covered taxes to the extent they are in lieu of a generally applicable income tax.

In several European countries the IPT liability lies with the insured party, even if the tax is collected by the insurance company. An example of taxes levied on insurance premiums that operate as a substitute to CIT is the French contribution on corporate added value (CVAE), which is recognised as an income tax under IFRS rules.

Questionnaire

Insurance Europe has not attempted to answer every question in the consultation, but provided answers to those questions of most importance to the insurance industry.

Chapter 1: Introduction and Executive Summary

a. GILTI co-existence. [Refers to paragraphs 25-28 of the Blueprint]

Q2: What are the interactions between GILTI and the GloBE rules that would need to be coordinated and how should they be coordinated?

- The implementation process of GloBE should include effective provisions to address any double taxation situation stemming from the application of both US GILTI provisions and GloBE rules among entities of a same MNE.

Chapter 2: Scope of the GloBE rules

a. The treatment of investment funds (as defined in Section 2.3.) under the GloBE rules. [Refers to paragraphs 76-83 of the Blueprint]

Q2. In the case of an investment fund under the control of an MNE Group, what additional rules would be needed to ensure the tax neutrality of the fund and ensure that:

- i. the MNE Group's share of the fund's income is not excluded from the GloBE tax base? And
- ii. related party payments to and from the fund cannot be used to circumvent the UTPR?

- Many life insurers consolidate the funds they invest in. These funds are used to pool investments from multiple policyholders investing through the insurer. Typically, the funds will directly back policyholder liabilities, so in the group result there will be a low shareholder profit related to this investment income. There may also be third-party investors (individual or corporate) who also invest in the same fund, particularly where an insurer has provided seed capital.

Example:

	Lux Fund	UK Life Insurer	Consolidated Group
<i>Gross Income</i>	100	100	100
<i>Policyholder liability increase</i>	0	(95)	(95)
<i>Profit Before Tax</i>	100	5	5
<i>Tax (0%/20%)</i>	0	(1)	(1)
<i>Profit After Tax</i>	100	4	4
<i>Distribution to investors (UK life insurer)</i>	100		
<i>Income inclusion rule tax overlay (10%) levied by UK authority</i>	(10)		(10)
<i>Total tax levied</i>	(10)	(1)	(11)

- The application of a top-up tax in this situation would clearly lead to an unfair situation.
- Regulatory rules for commercially run funds mean that life insurers can invest in strictly controlled asset classes.
- If there is concern about the use of these funds to circumvent the UTPR, the issue could be mitigated by assigning the fund's income to the investor where consolidation into the MNE group occurred due to investment by a regulated insurer that was subject to an IIR regime.

Chapter 3: Calculating the ETR under the GloBE Rules

a. Treatment of dividends and gains from disposition of stock in a corporation. [Refers to paragraphs 181-191 of the Blueprint]

Q1: Do you have any views on the appropriate ownership threshold and the methodology of how to determine that threshold, both for the exclusion of portfolio dividends and the exclusion for gains and losses on the disposition of stock from the GloBE tax base?

- The threshold for the exclusion of dividends should be in line with the EU Parent Subsidiary Directive. Dividends should therefore be excluded from the income if the shareholder owns at least 10% of the dividend-paying company. The 10% threshold is common among EU member states and functions as a role-model for non-European countries too. As a result, the 10% ownership test is well practiced and could be integrated in the Pillar Two rules relatively easily.
- In order to achieve the goal of administrable rules and low compliance burdens, there should be no distinction between domestic and foreign participations for an ownership threshold test (see paragraph 185 of the OECD Pillar Two Blueprint). Such a distinction could also violate the EU principle of free movement of capital.
- If a shareholder meets the criteria for the exclusion of dividends it is discussed whether expenditure corresponding to those dividends should be added back to the tax base for the purposes of Pillar Two (see paragraph 185 of the OECD Pillar Two Blueprint). Though from a systematic perspective such a corresponding rule might be comprehensible, from a practical perspective such a rule would be burdensome. Furthermore, the industry does not expect a noticeable effect on the tax base and the ETR. Therefore, there should be no add-back of expenditure corresponding to exempted dividends.
- Alternatively, expenditure corresponding to exempted dividends could be measured as a fixed percentage of the dividend amount, for example, in line with the Parent Subsidiary Directive 5% of the excluded dividend could be deemed a non-deductible expense.

Chapter 4: Carry-forwards and carve-out

- a. **Treatment of pre-GloBE losses and excess taxes under the carry-forward approach.** [Refers to paragraphs 315-318 of the Blueprint]

Q1: What technical issues should be taken into account in developing a rule that would recognise the impact of pre-regime losses and benefit of taxes paid by the Constituent Entities of an MNE Group prior to becoming subject to the GloBE rules?

- The European insurers are of the opinion that a deferred tax approach to capturing temporary differences is likely to be appropriate, however this will require careful application and some adjustments to avoid unfair or adverse outcomes.
- Insurance Europe believes that pre-regime losses must be properly accounted for. The inclusion of an MNE group within the scope of the GloBE rules would otherwise convert what is essentially a timing difference into a permanent difference simply because such losses occurred before the new regime was established, putting an MNE group at risk of being overtaxed.
- Therefore, Insurance Europe endorses the efforts to develop transition rules and reduce complexity (especially given the complex nature of the GloBE provisions), although the Report itself indicates that further technical work will be necessary to develop a workable solution that provides for appropriate outcomes without imposing undue compliance or administrative burdens.
- The industry is concerned that efforts to simplify the approach could result in an inconsistent measure of pre-regime losses and local tax carry-forwards relative to the future GloBE tax liability determinations against which such pre-regime amounts would be applied.
- European insurers would support the application of the identified “most accurate” approach, that is to identify an applicable start date for the transitional period and require an MNE group to compute an opening balance of its loss carry-forward and local tax carry-forward as if the GloBE rules had applied during the transition period, together with the optional “simplified method”, whose application would be left as an option for MNE groups (eg where an MNE group is not disadvantaged by the less accurate approach and/or wishes to reduce complexity and its administrative burden).
- Insurance Europe would also support the adoption of transition periods for pre-regime losses and local tax carry-forwards that are based on the provisions that would apply subsequent to the date on which the GloBE provisions are first applied to an MNE group (ie the “post-implementation” provisions), as they would ensure consistent outcomes from the application of the GloBE provisions.
- The post-implementation loss carry-forward is crafted so that it is effectively unlimited in duration, in acknowledgement of the fact that the GloBE rules apply to a wide range of sectors with varying business

cycles (including some sectors, such as insurance, that experience very long business cycles). There does not appear to be a compelling reason why the policy rationale supporting the indefinite carry-forward of post-implementation losses would not be equally applicable to pre-regime losses, other than the potential administrative burden associated with applying the GloBE provisions to a longer pre-regime transition period. As such, the insurance industry suggests that an MNE Group should be permitted to apply the “most accurate” approach to an indefinite period preceding the date on which the GloBE provisions first apply to such an MNE group. In practice, certain MNE groups may opt to limit the application of the “most accurate” approach to a shorter period (eg where insufficient records are available in support of a longer look-back period and/or the MNE group wishes to reduce its administrative burden by limiting the look-back period). However, the option to employ a longer transition period would be an effective and consistent means of addressing concerns that may arise in applying the GloBE provisions to sectors with longer business cycles and/or jurisdictions that provide for longer (or indefinite) local tax loss carry-forward periods.

- If it is determined that an indefinite transition period is not appropriate, it is essential that the period is long enough to address the concerns identified above. Insurance Europe believes that a minimum of 10 years would mitigate the potential for unintended GloBE outcomes from sectors with longer business cycles. The insurance industry would further suggest that an adjustment be permitted to increase the GloBE loss carry-forward amount to the extent that the loss carry-forward available to a constituent entity under local tax law exceeds the loss carry-forward determined with respect to the limited transition period.
- Accordingly, in determining the pre-regime local tax carry-forward Insurance Europe would suggest that an MNE group should be permitted to apply the “most accurate” approach to a transition period consistent with the post-implementation local tax carry-forward period (currently proposed at 7 years, per paragraph 310 of the Report). In practice, certain MNE groups may opt to limit the application of the “most accurate” approach to a shorter period (eg where insufficient records are available in support of a longer look-back period and/or the MNE group wishes to reduce its administrative burden by limiting the look-back period).

b. Formulaic substance-based carve-out. [Refers to paragraph 332-370 of the Blueprint]

Q1: Do you have any comments on the overall design of the carve-out?

- The Pillar Two Blueprint proposes an adjustment to carve out from the Pillar Two tax base a fixed return based on a payroll component and a tangible asset component. This formulaic carve-out has the effect of allowing routine returns to be sheltered for both labour-intensive and capital-intensive businesses.
- In the case of financial services companies, and more so in (re)insurance business, regulators already require specific and quantifiable amounts of capital to be held in specific entities to ensure the protection of policyholders. Therefore, there are rules in place to define how much capital is required to be in a given jurisdiction. Highly regulated financial services companies such as (re)insurance undertakings can decide where to pool risks most efficiently, but once the location of risk is determined it is difficult to move.
- Insurance Europe supports an economic substance exemption for financial services companies and, more specifically, for (re)insurers that reflects the realities of their business model – and therefore is based on regulatory capital.
- The carve-out proposed in the Pillar Two Blueprint is only appropriate for labour-intensive and tangible asset-intensive businesses, and therefore provides little benefit to the financial services industry.

c. Computation of the ETR and top-up tax. [Refers to paragraph 371-375 of the Blueprint]

Q1: Do you have any comments on the proposed calculation of ETR and top-up tax?

- The proposed effective tax rate (ETR) is calculated on a jurisdictional basis by dividing covered taxes by the amount of income within the company’s financial accounts that are prepared under the same accounting standard that is used by the parent, with certain adjustments.

- If timing differences caused by a regulatory basis of taxation in determining the tax base and covered taxes are not appropriately accounted for, there will be a mismatch in each jurisdiction's ETR between the basis used for the numerator (cash basis) and denominator (book basis).
- In the case of insurance, reserves (that is liabilities to pay future benefits to policyholders) can take decades to be taken off the books. Reserves represent the largest liabilities on an insurance company's balance sheet – and are generally multiple times larger than an insurance company's shareholders' equity capital.
- Because of this, the insurance industry may be impacted by the way ETR is calculated far more than other industries. There are often different rules to calculate these liabilities, and a small accounting difference for such a large balance sheet item can create enormous timing differences.
- The proposed alternative use of a carry-forward model will not reduce the distortions, administrative cost and compliance burden that the exclusion of timing differences creates. The European insurers urge instead consideration of a more accurate and straightforward model that includes deferred tax accounting.
- The examples below show that an insurance company with typical reserve liabilities would not benefit from the Pillar Two Blueprint's carry-forward proposal. An IIR tax credit or local tax carry-forward in cases where ETR in the origination year is below the minimum tax rate would not be created until the reversing year. This could be long after the year in which the top-up tax is paid for reserve differences for a growing business or long duration insurance products. Moreover, so long as an insurer maintains a steady book of business, or increases its book of business, reserve differences do not reverse in the financial statements. Again, this means the IIR tax credit or loss carry-forward would be ineffective in eliminating the effects of this timing difference. In contrast, incorporating deferred taxes through a regulatory tax basis calculation methodology would remedy this volatility by creating basis parity between the Pillar Two ETR's numerator and denominator.

Example 1

There is a basis tax adjustment due to the inclusion of additional prudence in the regulatory insurance reserves in accordance with the requirements of local insurance regulations.

Item	Origination year		Reversing year	
	Current OECD proposal	Tax base	Current OECD proposal	Tax base
Pre-tax income – group GAAP	1,000	1,000	1,000	1,000
Tax basis adjustment	(600)	600	(600)	600
Jurisdictional taxable income	(400)	400	(1,600)	1,600
Jurisdictional taxes at 22%	88	88	352	352
Deferred taxes	0	(132)	0	(132)
Covered taxes	88	220	352	220
Pillar Two ETR	8.80%	22.00%	35.20%	22.00%
Top-up tax (12.5% min rate)	3.70%	0.00%	0.0%	0.00%

Note the IIR tax credit carry-forward or local tax carry-forwards do not provide any benefit in this example, as there is no further Pillar Two IIR top-up tax liability. This, therefore, is a permanent additional tax.

A tax base adjustment such as this will commonly arise in the case of equalisation reserves, sometimes referred to as contingency or safety reserves. These are common in the insurance industry, particularly in EU countries, to create a financial "buffer" over and above the liabilities that are created for policyholder reserves. Even where Solvency II has superseded the national regulatory rules, tax rules often still follow the traditional regulatory basis of calculating insurance reserves. In general, equalisation reserves are required by regulators to be set aside to ensure that an insurance company maintains enough resources to fund future expected policyholder payments. The reserves are formulaic, incorporating an insured's premium income levels and the difference between the current period's claim activity and normalised claims activity, subject to a cap. As a result, an insurance company is required

to increase equalisation reserves in “good” years, which are then used to fund policyholder payments in “bad” years. Generally, increases to equalisation reserves are tax deductible and decreases in equalisation reserves are included in taxable income, thus equalising results over time. In general, there is no time limit after which unused reserves are returned to general funds. The equalisation reserves fully reverse only if/when the insurance company winds down its affairs.

Example 2

Mark to market movements are included in the regulatory return/tax base. However, as unrealised gains are taken to Other Comprehensive Income for accounting purposes, they are not included in the accounting pre-tax income until the gains are realised and amounts are recycled to the P+L.

Item	Origination year		Reversing year	
	Current OECD proposal	Tax base	Current OECD proposal	Tax base
Pre-tax income – group GAAP	1,000	1,000	1,000	1000
Tax basis adjustment	(600)	600	(600)	(600)
Jurisdictional taxable income	(1,600)	1,600	(400)	400
Jurisdictional taxes at 22%	352	352	88	88
Deferred taxes	0	(132)	0	(132)
Covered taxes	352	220	88	220
Pillar Two ETR	35.2%	22.00%	8.80%	22.00%
Top-up tax (12.5% min rate)	0.00%	0.00%	3.70%	0.00%

Note in the example above that the carry-forward attributes (which are time-limited unlike losses) are presumed to have expired due to the long-term nature of insurance business and are hence not available in the reversing year.

The result in example 2 above is that excess taxes are generated in the originating year, with Top-Up Tax generated in subsequent years. The Blueprint does propose a tax carry-forward mechanism for the excess taxes generated in the originating year. However, the Blueprint indicates there will only be a limited carry-forward of excess taxes, and given the unpredictability of mark-to-market fluctuations and the long-term nature of insurance business, it is very possible that that the excess tax carry-forwards will expire before they can be used.

In some tax/accounting combinations the impact of mark-to-market movements will be reversed, with them being included in accounting but not tax results, with the difference unwinding only on realisation of the asset.

- For the reasons provided above, Insurance Europe asks that that the significant tax/accounting differences are considered and dealt with appropriately. The insurance industry favours deferred tax, as this eliminates significant timing differences due to differences in the valuation of investment assets and insurance liabilities between tax and accounting results in a well understood manner. Any concern over the ability to control deferred tax impacts could be overcome by providing this as an option for investment assets and insurance liabilities within regulated insurers only.

Chapter 5: Simplification options.

- a. **General. The Blueprint describes four potential simplification measures, including (i) Cbc Report ETR safe harbour, (ii) de minimis profit exclusion, (iii) single jurisdictional ETR calculation to cover several years, and (iv) tax administrative guidance.**

Q3: Can you identify any other overall simplification measures that could be explored by the Inclusive Framework or potential simplifications to the design or application of specific elements of the IIR or the UTPR that would not undermine their objective or effectiveness?

- All the tax expenses of MNEs should be taken into account in the ETR calculation for the purposes of the GloBE rules. In that respect, the most efficient way of addressing the specific timing differences implied by the (re)insurance cycles of losses and gains is deferred taxes accounting.

b. CbC Report ETR Safe Harbour. [Refers to paragraphs 381-390 of the Blueprint]

Q2: Do any of the required adjustments, as described in the Blueprint, create significant additional complexity? Do you have any suggestions on how to streamline these required adjustments?

- This simplification measure would be more effective with very few adjustments. Therefore, the industry could endorse a reviewed CBCR that would allow it to be used as basis for ETR calculation under the GloBE rules unadjusted.

c. De minimis profit exclusion. [Refers to paragraphs 391-398 of the Blueprint]

Q5: In order to be effective, how should the de minimis threshold be set? Should it be a percentage of group profit, a fixed monetary amount threshold, or a combination of the two?

- The de minimis profit exclusion rule should work as a relative threshold based on the global profit of the MNE. The 2.5% proposed rate in the Blueprint enables MNEs to exclude entities that would normally not be taken into account in the consolidated financial statements.

e. Tax administrative guidance. [Refers to paragraphs 404-409 of the Blueprint]

Q5: Do you have any additional comments regarding this simplification, including how it could be improved to offer greater simplification and certainty?

- Having a list of either high or low-risk jurisdictions would be very helpful to narrow down the amount of ETR calculations for large MNEs.

Chapter 6: Income Inclusion and Switch-over rules

c. Split-ownership. [Refers to paragraphs 434-452 of the Blueprint]

Q1: Do you have comments on the design of the proposed split-ownership rules?

- In the case of split ownership, insurers understand that under the GloBE rules MNEs may be subject to multiple IIR liabilities, concerning the UPE and partially-owned intermediate parents. This would only increase the administrative and compliance costs of implementing Pillar Two. It would be far easier if any IIR liability provided for under GloBE rules were dealt with by the UPE only.

Chapter 9: Subject to Tax Rule

a. Covered payments and low-return exclusion. [Refers to paragraphs 588-616 of the Blueprint]

Q1: Do you consider that the categories of covered payments and the exclusion for low-return payments ensures that the STTR focuses on the transactions that present significant BEPS risks?

- Insurance Europe is concerned by the inclusion of insurance and reinsurance premiums in the definition of covered payments under the subject to tax rule (STTR), as BEPS risk payments. This seems at odds with the purpose of the STTR, which should not be applicable to normal, regulated business transactions. The industry urges the IF to exclude insurance and reinsurance premiums from the scope of the STTR rule, in so far as they meet the criteria of genuine insurance business as defined in the OECD Transfer Pricing Guidelines.
- To the extent intragroup insurance premiums are subject to the STTR withholding, the industry believes that the nature of insurance premiums should be distinguished from other intragroup payments. The STTR relating to insurance or reinsurance premium seems to disregard the economic realities in the insurance sector and would likely result in over-taxation.
- Paragraph 601 and 602, as currently drafted, do not consider the nature of insurance (and reinsurance) and how the global industry operates in a highly regulated environment. Critically, the inclusion of the

sentence "If the risk does not materialise, the insurance or reinsurance premium can generate a high return." in the consultation misses the whole point of insurance. If the risk does materialise, a loss far exceeding the initial premium payment can arise, ie the risk of the adverse event occurring has been assumed by the insurer.

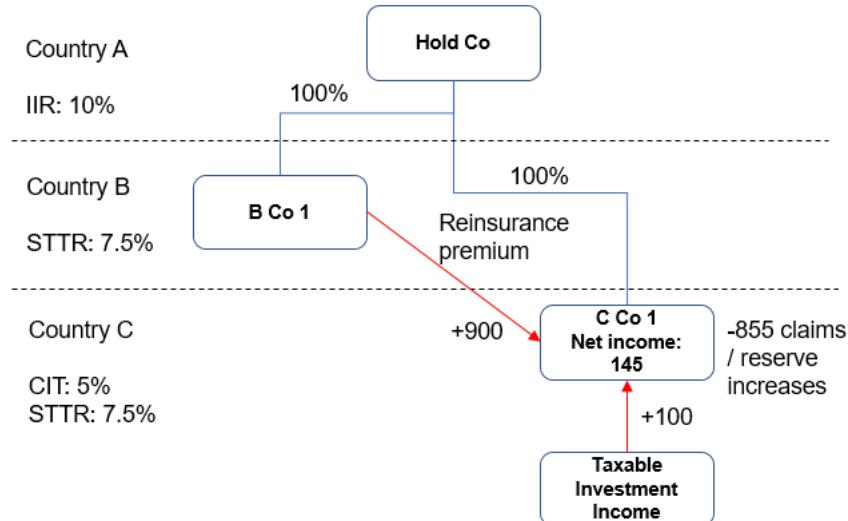
- Insurance premium payments do not correlate to corporate profitability/profit transfer in the same way that interest or royalty payments do. In fact, an insurer can receive substantial premiums even where business is ultimately loss-making.
- Substance for an insurer is intrinsically linked to appropriate capital being held in a regulated legal entity. The minimum amount of capital required is set by the local regulatory authority, however the attitude of ratings agencies and insurance counterparties means, in practice, prudence on top of this minimum must be retained by an insurer. This capital is not very fungible, and regulatory rules acknowledge this when looking at the overall group capital position for insurers.
- The accounting result (eg IFRS) does not lead directly to free cash generation; this depends on the regulatory rules on capital. This is one of the reasons why tax rules often follow a regulatory basis with different rules for valuing investment assets and insurance liabilities. As these comprise the significant items on an insurer's balance sheet, this commonly leads to timing differences between tax and accounting results in the hundreds of millions or billions of dollars, as can be seen by the size of deferred tax assets/liabilities on insurers' balance sheets.
- Many insurance policies extend over decades. This is common in both the long-term savings world (eg pensions and investment bonds) and general insurance (eg asbestos claims that arise decades after the associated premium payments).
- Combining these tax and business impacts means that insurers have extended timing differences which may take decades to reverse.
- Large claim events (eg hurricanes) and market movements in one year can lead to losses that take many years to recover. Insurers operate a long-term view as part of their business planning. Profitability in any given period is not the key metric – it is the long-term trend.
- Additionally, in relation to the STTR Insurance Europe underlines the following aspects:

Risk of substantial over-taxation

- The envisaged withholding tax potentially leads to over-taxation because it would be levied on the gross amount of a payment. This would hit particularly hard those companies whose sole or main source of turnover was subject to withholding tax under the envisaged STTR, as would often be the case for reinsurers of MNE insurance groups. A likely consequence would be that the withholding tax would push the effective tax rate in the payee jurisdiction far above the minimum tax rate, resulting in a perpetual building up of the local tax carry-forward in the insurer jurisdiction which can never be used.
- An example is provided below to show the over-taxation effect of the STTR. It cannot be seen as a one-off event in a single year, but rather as a more or less prevailing situation. The Subject To Tax Rule would work as a turnover tax, possibly in addition to an insurance premium tax levied on the same payment. This would result in penal tax where losses result and cannot be justified as a BEPS countermeasure.

Example (based on Blueprint example 10.2.1A):

- B Co 1 pays 900 of reinsurance premiums to C Co 1.
- Country C has a corporate tax rate of 5%.
- C Co 1 also has 100 taxable investment income.
- Income of C Co overall is 145 (The combined ratio, ie losses and expenses as a proportion of premium, is 95%, giving an underwriting profit of 45 (5% of 900) to add to the investment income of 100).
- Hold Co is subject to an Income Inclusion Rule in Country A. Countries B and C have a tax treaty that follows the OECD Model Tax Convention and contains a STTR.
- The minimum adjusted nominal tax trigger rate for the purposes of the STTR is 7.5% and the minimum rate for the GloBE rules is 10%.



- A 2.5% (7.5% - 5.0%) STTR withholding (=22.5 tax) applies to the reinsurance payment from B Co 1 as the country C nominal tax rate is lower than the 7.5% trigger rate.
- C Co 1 suffers a 5% local tax charge (=7.25 tax) on the tax base (profit) of 145.
- Total covered taxes for C Co 1 are 29.75 giving a total rate of 20.5%.
- The IIR does not apply at Hold Co level as the total rate is 10.5% above the IIR minimum tax rate of 10%, with 15.25 of additional tax charged. This results in a local tax carry-forward.
- If only the IIR rule were applied, only an additional 5% Pillar Two IIR tax (= 7.25 tax) would have been triggered at the HoldCo level, giving a total ETR of 10%.

Critically, assuming similar reinsurance premiums and profitability in future periods, the STTR withholding will routinely swamp any possible IIR top-up. The local tax carry-forward would only be used where the reinsurance volume fell significantly, or profitability was far higher than the assumed 95% combined ratio.

Differentiation in view of BEPS risks between captives and reinsurance entities of insurance MNE groups

- The undifferentiated inclusion of (re)insurance premiums in the high-risk service category seems unfounded and would have undesirable economic effects on legitimate business models in the insurance sector. The examples of captives mentioned by the OECD are not comparable to the business model of globally operating insurance companies. From a BEPS risk perspective, a distinction should be made between a captive and a reinsurance entity of an insurance MNE group. A captive, on the one hand, typically provides insurance policies exclusively or almost exclusively for risks of entities of the MNE group to which it belongs. A reinsurance entity, on the other hand, provides reinsurance for risks of unrelated parties that are insured by other entities of the MNE group to which it belongs. This is a genuine and normal part of the business model of insurance groups. The reinsurance entity is a regulated company and is therefore subject to regulatory capital requirements which ensure that it has the financial capacity and the necessary personnel to assume risks from the insured customers. Substantial losses may occur at any time and are part of the course of business. Usually, besides providing intra-group reinsurance to other group members, the reinsurer of an insurance MNE group has predominantly direct business with third-party customers.

Transfer pricing comparables are available

- It also follows from the above that comparable uncontrolled prices are available from contractual arrangements with third-party customers. The assumption in section 601 of the Pillar Two Blueprint

that it would be hard to find comparable unrelated transactions to test whether the pricing of intra-group transactions meets the arm's length principle seems unfounded when it comes to reinsurance entities of insurance MNE groups.

- Furthermore, since the new chapter X of the OECD Transfer Pricing Guidelines with a section dedicated to captive insurance has been adopted, there are existing international transfer pricing rules that address low substance captive structures, effectively mitigating the risk of artificial BEPS resulting from (re)insurance transactions.

Detimental effect on economically driven business models and group structuring

- The Subject to Tax rule would penalise the internal (re)insurance structures of MNE groups which are an essential means to achieve an allocation of capital and risk that meets market requirements. Such structures are required to address requirements imposed by regulators worldwide, which seek to ensure an as-high-as-possible capital endowment of (re)insurers to protect the insured against the potential default of their insurance policies. A less efficient allocation of (costly) capital and risk, and an additional cost component by an imposed withholding tax on (re)insurance premiums would increase the pressure on prices of end-consumer insurance products which is already affected by increasing withholding tax requirements worldwide. The level of taxation is not the decisive factor for locating a reinsurance entity of an MNE group in a certain jurisdiction.
- The withholding tax under the Subject to Tax rule would work as a disincentive to spreading insurance risks among group members, since it raises the costs for buying intra-group reinsurance policies. The consequence may be the accumulation of insurance risks in countries that have introduced the Subject to Tax rule.

Subject to Tax Rule would make insurance policies more expensive

- An additional tax on the payment of (re)insurance premiums would impose an additional cost on the (re)insurance product. It is in the fundamentals of (re)insurance business that fixed and expected costs, including a claim, must be covered by premiums. Consequently, increasing fixed cost elements to (re)insurance has a direct effect on the pricing of (re)insurance products.

Compliance burden as a result of the Subject to Tax Rule

- Furthermore, the withholding tax leads to an administrative burden since a compliance system has to be set-up on a worldwide basis to monitor and administer the withholding taxes paid.

Q2: Do you have any views on the design and practical application of this rule component as well as potential simplifications?

- Intra-group insurance and reinsurance premiums of MNE groups in the insurance sector should be removed from the scope of the STTR rule. Alternatively, over-taxation effects should be eliminated by allowing unusable local tax carry-forwards resulting from STTR — withholding tax to be credited against income tax liabilities in the UPE jurisdiction.

b. Materiality threshold. [Refers to paragraphs 623-636 of the Blueprint]

Q1: What are your views on including a materiality threshold?

- The European insurers support a single consolidated revenue threshold of €750m for the purposes of applying the GloBE provisions.
- Should jurisdictions have the option to introduce an IIR that applies to groups with consolidated revenue of less than €750m, many MNEs will struggle to aggregate the necessary data and perform the relevant analysis to apply the GloBE provisions, and Insurance Europe would anticipate that these challenges will be particularly acute for smaller groups. While even larger MNEs have expressed concerns regarding

- the administrability of the GloBE rules, these concerns are mitigated by efforts to ensure that these provisions represent a multilateral solution, consistently applied on a global basis. The introduction of jurisdictional optionality regarding a lower IIR revenue threshold creates additional uncertainty and complexity, while making it more difficult to coordinate the global application of these provisions and setting a concerning precedent for potential departures from a multilateral approach.
- The focus on a jurisdictional blending approach has been a significant contributing factor to the complexity and administrative burden associated with the proposed GloBE rules. Insurance Europe feels that global blending provides a more appropriate balance between the policy objectives of the GloBE provisions and overall administrability of such provisions and continue to support global blending as the preferable alternative to jurisdictional blending. The deference and acknowledgement to GILTI support alignment with global blending as the international standard.
- The insurance industry acknowledges the OECD preference for a jurisdictional basis, but advocate that using a global calculation as a safe harbour (eg at a higher rate than the GloBE minimum) could provide a welcome simplification and remove the costly compliance complexity for many groups operating predominantly in high-tax jurisdictions.
- Moreover, admitting the materiality standard used for the purposes of preparing the UPE's consolidated financial statements would achieve consistency of accounting rules. There would be no need to resort to entity-level financial information for subsidiaries not catered for in the MNE's financial statements and therefore no discrepancy in accounting standards.

Chapter 10: Implementation and rule co-ordination

a. Effective co-ordination of the GloBE rules. [Refers to paragraphs 697-708 of the Blueprint]

Q1: Are there any co-ordination mechanisms or other features of the GloBE that you would suggest exploring in order to provide for more tax certainty in applying the Pillar Two rules?

- Due to the complex rules under Pillar Two, there will be an inevitable increase in the compliance burden for companies as well as tax authorities. To offset at least part of the additional compliance burden, the introduction of the rules should be accompanied with a cutback of existing anti-abuse rules with similar policy objectives. The envisioned rules already secure an effective minimum taxation of the (global) income of companies that are in the scope of Pillar Two. Due to the applicable minimum taxation, as well as the increased compliance burden, exemption should be considered for these in-scope companies from comparable national anti-abuse rules. Otherwise, the simultaneous application of national anti-abuse rules and the GloBE rules may result in double taxation as well as unnecessary bureaucratic expenditures.

b. Dispute prevention and resolution. [Refers to paragraphs 709-715 of the Blueprint]

Q1: In addition to the design features and proposed approach to implementation of the IIR and UTPR, what additional options do you think should be considered to minimise the scope for double taxation and dispute?

- Given the various types of tax regulations that may apply to MNEs worldwide, the interaction between such different rules may result in conflict-of-law issues and litigation. Most MNEs already experience such situations and go through existing dispute settlement schemes such as bilateral MAPs. It is very likely that the GloBE proposal, by designing a global minimum income tax, would increase the risk of legal disputes, due to divergent understandings of those rules by local tax authorities or a mismatch between international and domestic rules.
- Therefore, the industry supports the development of a multilateral convention introducing provisions for dispute prevention and resolution.
- Robust dispute prevention and resolution schemes should be considered in the GloBE proposal, as well as reasonable timelines in order to allow settlement within timeframes that would not hinder business and provisions for the exchange of information between tax administrations.