Group 4: Pillar 2 : Intégration of consolidated accounts into Taxation

Part 1: Organizational challenges within a corporate group

In october 2021, 136 countries in the world, members of OECD adopt a reform plan. It is called GloBE : Global Anti Base Erosion Rules. The objective is to fight against Base Erosion Profit Shifting. The plan aims large multinational entreprises. So it is based on two Pillars. Pillar 1 creates a new right to tax multinational companies. Pillar 2 creates a minimum tax rate. This rate has to be effective, which means that the company has to pay 15% tax on its income, no matter what is the rate in the law. Pillar 2 is an internationnal standard so all the countries that adopt it have to implement it in their legislation. In France, it has been implemented with the budget act in 2024. The measure has been transposed in France and Italy in a very faithful manner,so there is a real harmonization of this mechanism.

So first, we are going to see the Organizational challenges within a corporate group. Then, why tax teams can no longer work in isolation from consodilation teams, the impact of tax requirements on financial reporting and to finish, how this trend breaks down silos beetween tax and financial consolidation departments.

What companies are we talking about ?

There are two criterias to be subject to Pillar 2 :
-the company has an international presence : it means that the group has at least two entities in two different jurisdictions
-turnover treshold : the treshold is 750 millions in the world, the point of this treshold is avoding slowing down the development of small companies. It is assessed over 4 years.

The rules
The application of Pillar 2 results in two rules :

Rule n°1 : Income Inclusion Rule

We calculate every effective tax rate in every jurisdiction where the company has an activity. If the rate is under 15%, we can apply the rule. The company will pay an additional tax to reach 15% of its income. This tax will be payed by the Ultimate Parent Company to the country where it is established. This is the Ulimate Parent Company that is liable because it avoids double taxation, this is simpler.

If the Ultimate Parent Company is not subject to the Income Inclusion Rule, the tax will be levied at the level of an intermediary company, the one that is just under the Ultimate Parent Company.

Rule n°2 : Undertaxed Payment Rule

This rule is used after the rule n°1, because it is useful when IIR has not been applied. It is a « catch up mechanism ». For example, if the Ultimate Parent Company is established in a country that has not adopted the mechanism, and if the IIR can't be applied to the intermediary company, the UTPR can be used. There are two ways of application : the jurisdiction can refuse a tax deduction or institute an additionnal tax.
So this device can reduce competition beetween states. Indeed, a state will not have any advantage in taxing at a low rate because the tax will be payed by the company anyway, but it will be an other country that will benefit from the tax.

Challenges

The introduction of Pillar 2 by the OECD represents a major shift in global taxation. This regulatory change directly impacts the integration of consolidated accounts into taxation, requiring companies to align their financial reporting with new tax compliance obligations.

For corporate groups, this transition presents significant organizational challenges. The need to reconcile financial consolidation with tax calculations imposes structural, technological, and procedural changes. Multinationals must now navigate complex adjustments in tax reporting, intercompany transactions, and financial transparency.

First, there will be relocation and restructuration of activities. Indeed, jurisdictions with low tax rate will lose their attractivness. Many companies have subsidiaries in some jurisdiction only because of the low tax rate. So maybe if the company will pay the difference anyway, the activity will be moved in an other country with better operationnal efficiency.

Then, the transition to a Pillar 2-compliant tax system requires significant technological upgrades : companies have to update their accounting software to calculate their effective tax rate because if they don't reach 15% they have to pay an additionnal tax so now this rate has to be considered. It involves centralization of tax data to be sure that every jurisdiction collects the right amount of tax, and integrating tax compliance modules within financial software to automate minimum tax calculations.

Better coordination is needed beetween subsdiaries and Ultimate Parent. Reporting entities must provide jurisdiction-specific tax disclosures, increasing the need for detailed and accurate financial segmentation. Consolidated accounts must reconcile with Country by country data to ensure consistency in tax and financial reporting.

There will be adjustments in transfert pricing and intercompany accounting.

Multinational groups face major governance shifts as they implement Pillar 2 regulations. Companies must determine whether to centralize tax compliance functions at the headquarters or distribute responsibilities across subsidiaries. Strengthening internal tax governance structures to ensure adherence to the new minimum tax requirements.

Another point is training and Skill Development. Multinational will need upskilling tax professionals and finance teams to handle new compliance requirements and strengthening collaboration between tax, finance, and legal teams to navigate cross-border tax complexities.

Part 2: Why Tax Teams Can No Longer Work in Isolation from Consolidation Teams

Historically, tax teams and consolidation teams worked separately. Tax specialists focused on local tax obligations and declarations, while consolidation teams were responsible for preparing financial statements according to IFRS or national accounting standards.

However, this separation is no longer viable due to new international regulations, particularly Pillar 2, which imposes a minimum effective tax rate of 15%, calculated based on consolidated accounts for multinational companies.

This means that a group's tax liability can no longer be calculated independently of its consolidated financial statements, making collaboration between these two functions essential.

The question we need to ask is: Why can tax teams no longer work in isolation from consolidation teams, and how does this evolution manifest in France and Italy ?

First, we will examine why tax teams can no longer work in isolation from consolidation teams. Then, we will analyze how this evolution is taking place in France, where the tax and accounting framework is becoming increasingly interconnected.

Finally, we will look at the case of Italy, which stands out for its enhanced tax transparency and strict compliance rules.

I. The French Perspective: Growing Interconnection Between Tax and Consolidation

French companies are required to prepare consolidated financial statements in accordance with IFRS standards for listed companies and CRC 99-02 (ninti nine zero two) regulations for other groups. At the same time, the fiscal integration regime allows groups to optimize their taxation by consolidating their results for tax purposes.

However, with the introduction of Pillar 2, tax authorities will now assess whether a group's overall tax burden meets the 15% (fifty pourrcent) threshold based on consolidated data. This means that tax teams must rely on the information produced by consolidators to correctly calculate the tax due.

For example, consider a French multinational that must report its global effective tax rate. If the consolidation team underestimates certain deferred tax assets, the effective tax rate may appear artificially low, which could trigger an additional tax payment under Pillar 2.

Poor communication between tax teams and consolidation teams can therefore have direct financial consequences. Ensuring close coordination helps prevent such errors and guarantees that consolidated data accurately reflects the group's tax reality.

The lack of coordination between these two teams also poses significant risks. First, discrepancies between accounting and tax adjustments can lead to errors in tax declarations, exposing the company to penalties.

Moreover, French tax authorities increasingly verify the consistency between tax declarations and consolidated financial statements. In the event of an audit, unexplained discrepancies may lead the tax authorities to requalify certain elements, resulting in tax reassessments and penalties.

Finally, poor integration of financial information can make it more difficult to justify discrepancies, complicating the company's defense in the event of a tax dispute.

A concrete example illustrates this risk well. Suppose a French company records a litigation provision in its consolidated accounts without the appropriate tax adjustment.

During an audit, the tax authorities may determine that this provision is not tax-deductible and impose an adjustment with late payment interest. Better communication between tax and consolidation teams would have anticipated this adjustment and avoided such a risk.

While France already enforces strict coherence between tax and consolidation data, Italy goes even further with particularly stringent tax regulations and increased scrutiny of discrepancies between accounting and tax data.

II. The Italian Perspective: Stricter Transparency and Compliance

In Italy, groups apply OIC accounting standards for non-listed companies and IFRS standards for listed companies. The country has implemented a fiscal consolidation regime called "Consolidato Fiscale Nazionale," which allows companies to optimize their taxation by consolidating their results for tax purposes.

However, under Pillar 2, Italian tax authorities require companies to precisely justify their effective tax rate, with any inconsistency between tax declarations and consolidated financial statements perceived as a red flag.

A concrete example illustrates this increased transparency requirement. An Italian subsidiary applies an innovation tax credit. In the consolidated accounts, this credit is immediately recorded as a tax reduction, whereas, for tax purposes, it must be spread over several years.

If the tax team does not account for this difference and fails to adjust it in the tax returns, the group's effective tax rate could be distorted, exposing the company to a tax reassessment.

This case demonstrates the importance of close collaboration between tax and consolidation teams to prevent such errors and ensure compliance with applicable rules. Italy also stands out with particularly stringent reporting obligations. The Italian tax authorities require detailed documentation to justify tax choices, especially under Pillar 2.

They enforce anti-abuse rules to prevent any artificial manipulation of the consolidated tax burden and systematically monitor discrepancies between consolidated accounts and tax declarations. In 3 the event of an unexplained discrepancy, authorities may view it as an attempt at tax evasion, with severe consequences for the company. A concrete example illustrates these risks well. An Italian company attempts to reduce its tax burden by overestimating its depreciation expenses in the consolidated accounts, artificially lowering its taxable base.

During a tax audit, the authorities detect this practice and impose an adjustment with penalties for tax fraud. This situation could have been avoided through better communication between tax and consolidation teams, who could have correctly adjusted these depreciation expenses before the tax declaration.

Conclusion : Pillar 2 is profoundly transforming the tax management of multinational groups by requiring tax calculations to be based on consolidated financial results. This new approach forces tax and consolidation teams to work together to ensure the consistency of financial and tax data. In both France and Italy, misalignment between taxation and consolidation can lead to major risks, ranging from simple tax adjustments to penalties for non compliance or even tax fraud. A smooth and continuous collaboration between these two departments is therefore essential to ensure optimized, transparent, and compliant tax management in line with international requirements. This is no longer just a recommendation but a strategic necessity for companies operating in a rapidly evolving tax environment.

Part 3: The impact of tax requirements on financial reporting and vice versa:

1. The impact of tax requirements on financial reporting:

I will discuss the global impact of tax requirements on financial reporting. I will therefore address the challenges this topic involves for both France and Italy.
The implementation of Pillar 2 of the OECD's Global Minimum Tax introduces new tax requirements that significantly impact financial reporting. These requirements affect how companies recognize, disclose, and report tax-related items in their financial statements.
In corporate governance, a key question is whether bilateral tax agreements (BTAs) enhance financial reporting quality by limiting corporate tax avoidance. International Tax Transparency Standards, including the Exchange of Information on Request, the Common Reporting Standard, and the Crypto-Asset Reporting Framework, have reshaped global tax compliance by curbing offshore tax evasion.Here are the key impacts:

1.Recognition and Measurement of Deferred Taxes

Companies must assess whether existing **tax losses or deductions** remain usable under the new regime.

Impact on Financial Reporting:

- Changes in deferred tax accounting may lead to **adjustments in balance sheets**.
- **Reassessment of tax loss carryforwards** based on new taxable income calculations.
- Companies must ensure **alignment between tax reporting and IFRS/GAAP accounting standards**.

2. Increased Disclosure and Transparency Requirements:

Pillar 2 mandates detailed **country-by-country reporting (CbCR)**.
Companies must **disclose the impact of Pillar 2 taxes** in financial statements.

In this sense , we can talk about the OECD Reporting Frameworks :

- Common Reporting Standard (CRS)
- Crypto – Asset Reporting Framework (CARF)
- Exchange of information on request (EOIR)

Example of the application of the OECD's will on transparency and new tax reporting obligations:

In France:

On January 24, 2025, the French tax authorities released a new form for Pillar Two filing and notification obligations, following the December 5, 2024 decree. The form requires details such as the ultimate parent entity's name, tax number, and the entity responsible for filing the group information return (GIR) and qualified domestic minimum top-up tax (QDMTT). It also includes a section for the domestic minimum top-up tax (DMTT) for French investment entities. Additionally, the form serves as a notification for country-by-country (CbC) reporting, previously part of Form 2065-SD. The form must be filed with the corporate income tax (CIT) return, due three months after the fiscal year end.

In Italy: On May 20, 2024, the Ministry of Economy and Finance issued a decree introducing transitional country-by-country (CbC) reporting safe harbors for groups subject to the Pillar Two global minimum tax, including multinational and large domestic groups with revenues over €750 million. These optional safe harbors apply during the initial phase of the global minimum tax rules, from 2024 to 2026, to ease compliance burdens. Groups can pass one of three tests (de minimis, simplified ETR, or routine profit test) to be considered low risk. This reduces the group's top-up tax to zero in a jurisdiction for that fiscal year, without calculating the effective tax rate (ETR) or any top-up tax.

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3. Impact on Cash Flow and Profitability Reporting :

⇒ Increased **tax payments** due to **top-up taxes** can **affect liquidity**.
⇒ Changes in **deferred tax recognition** impact reported **profitability and cash flow statements**.

Impact on Financial Reporting:

- Companies must disclose **how tax payments affect cash flow**.
- More focus on tax **provisions and contingencies** in financial reporting.
- Potential **impact on earnings per share (EPS)** and financial performance metrics.

Conclusion: Pillar 2 reshapes financial reporting by introducing new tax liabilities, disclosure requirements, and accounting challenges. Companies must adjust ETR calculations, reassess deferred tax assets, enhance financial disclosures, and upgrade tax reporting systems to ensure compliance.

4. The impact of financial reporting on tax requirements:

The OECD's second pillar has important implications for financial reporting and tax compliance. Financial reporting plays a crucial role in the development of tax requirements under this framework, as it determines the data used to assess the effective tax rate (ETR) and potential additional taxes.

1. Determination of Effective Tax Rate (ETR) for Minimum Tax Calculation:

⇒ Financial statements serve as the **foundation for tax calculations** under Pillar 2.

⇒ The **effective tax rate (ETR)** is calculated based on financial reporting figures, including **book profits** and **taxes accrued**.

⇒ Any differences between **accounting profits (GAAP/IFRS)** and **taxable income** may lead to **adjustments** under the Global Anti-Base Erosion (GloBE) rules.

⇒ **Impact on Tax Requirements:**

⇒ If an entity's **ETR is below 15%**, it must pay a **top-up tax** to reach the minimum threshold.

⇒ Companies must ensure **consistency between financial statements and tax filings** to avoid disputes.

2. Increased Tax Transparency and Compliance Burden:

Impact on Tax Requirements:

- Companies may need to **adjust internal reporting systems** to provide more detailed **jurisdictional tax data**.
- Tax authorities may require **reconciliations between financial reports and tax returns**.
- More **tax audits and compliance checks** could arise due to discrepancies in reporting.

Conclusion on the impact of financial reporting on tax requirements:

Pillar 2 fundamentally changes how **financial reporting influences tax obligations**. Companies must ensure **accurate reporting**, align tax strategies with financial statements, and prepare for **greater transparency and compliance demands**. The alignment between **financial reporting and tax requirements** will be critical in minimizing risks and **managing the global minimum tax impact effectively**.

Pillar 2 **adds significant reporting challenges** for companies operating across multiple jurisdictions. The biggest hurdles include **data standardization, tax reconciliation, deferred tax treatment, and increased transparency requirements**. To mitigate risks, MNEs should **invest in robust reporting systems, enhance collaboration between finance and tax teams, and proactively adapt their financial reporting frameworks**.

The impact of Pillar 2 on financial reporting is profound: changes to accounting standards, new transparency requirements, revised effective tax rates and effects on investor decisions. Companies are having to adapt their accounting and reporting to comply with increased tax requirements, thereby enhancing global tax transparency but making accounting and financial management more complex.