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Pillar Two Update - Securitisation Entities

Introduction

On 17 June last, the Organisation for Economic Co-operation and Development ("**OECD**") released further Administrative Guidance on the 'Pillar Two' Global Anti-Base Erosion ("**GloBE**") Rules (the "**Guidance**").

As anticipated, among other matters addressed therein, the Guidance specifically considers Securitisation Entities (as defined below).

While many Securitisation Entities will not be directly impacted by the OECD GloBE rules (as a result of not being a constituent entity of a group with annual consolidated revenue of at least EUR 750 million, or a standalone entity with revenue of at least EUR 750 million), for those Securitisation Entities that are directly impacted, the Guidance is of particular significance.

Background

The OECD GloBE rules, applicable to large multinational or domestic groups with annual consolidated group revenue of at least EUR 750 million, are designed to result in 'top-up' tax amounts payable in respect of profits of constituent entities of those groups, so that the overall tax on profits of the group applies at a minimum effective tax rate of 15%. This can be achieved by one or more of the following top-up taxes applying to constituent entities, where the effective tax rate would otherwise be less than 15%:

1. A qualified domestic minimum top-up tax (a **"QDMTT")**

This is a top-up tax levied on an entity by its taxing jurisdiction in respect of its undertaxed profits. Where this top-up tax meets certain conditions, known as the "consistency standard", a **QDMTT Safe Harbour** applies. The effect of a QDMTT Safe Harbour with respect to the profits of an entity is that the GloBE Rules in other jurisdictions (see 2 and 3 below) do not apply to those profits (as they might otherwise have applied to those profits, if the local jurisdiction had not imposed such QDMTT).

In addition, in certain limited prescribed circumstances where the outcome of such top-up tax would not otherwise meet the consistency standard, but where it would have a disproportionate impact if it were determined in relation to the top-up tax more generally that it does not meet the consistency standard to be a QDMTT on account of such outcome, instead, that the QDMTT Safe Harbour shall be disapplied, but only in those certain limited prescribed circumstances with respect to a group or a class of entities in a group, as the case may be. This is known as a "**Switch-off Rule**". In such a scenario, the QDMTT Safe Harbour is preserved for all situations other than where the Switch-Off Rule applies to switch off the QDMTT Safe Harbour for a group or a class of entities in a group, as the case may be, in those limited prescribed circumstances.

Ireland has implemented the option to introduce a top-up tax that is intended to meet the consistency standard to be a QDMTT.

2. An income inclusion rule (an **"IIR")**

This rule applies a top-up tax that is levied on a parent company by that company's taxing jurisdiction, with respect to its allocable share of profits of foreign branches and subsidiary entities of that parent company that are not sufficiently taxed in the host jurisdiction (and where a QDMTT Safe Harbour does not apply).

3. (from 2025) **An undertaxed payments rule (**a **"UTPR").**

This rule operates as a backstop to the IIR, i.e., a top-up tax will apply pursuant to the UTPR if not all top-up tax is allocated under an IIR. This is so as to achieve a minimum effective tax rate of 15% on all profits, if not otherwise achieved through IIR.

Securitisation Entities

For the purpose of the Guidance:

A "Securitisation Entity" means an entity which is a participant in a Securitisation Arrangement, and which satisfies all of the following conditions:
a. the entity only carries out activities that facilitate one or more Securitisation Arrangements;
b. it grants security over its assets in favour of its creditors (or the creditors of another Securitisation Entity);
c. it pays out all cash received from its assets to its creditors (or the creditors of another Securitisation Entity) on an annual or more frequent basis, other than:

i. cash retained to meet an amount of profit required by the documentation of the arrangement, for eventual distribution to equity holders (or equivalent); or

ii. cash reasonably required under the terms of the arrangement for either (or both) of the following purposes:

1. to make provision for future payments which are required, or will likely be required, to be made by the entity under the terms of the arrangement; or
2. to maintain or enhance the creditworthiness of the entity.

However, an entity shall not be treated as a Securitisation Entity unless any profit for a given fiscal year is negligible relative to the revenues of the entity.

A "Securitisation Arrangement" means an arrangement which satisfies the following conditions
a. it is implemented for the purpose of pooling and repackaging a portfolio of assets (or exposures to assets) for investors that are not entities of the group in a manner that legally segregates one or more identified pools of assets; and
b. it seeks through contractual agreements to limit the exposure of those investors to the risk of insolvency of an entity holding the legally segregated assets by controlling the ability of identified creditors of that entity (or of another entity in the arrangement) to make claims against it through legally binding documentation entered into by those creditors.

Application of Pillar Two Globe Rules to Securitisation Entities – New Guidance

QDLTT

The Guidance provides that jurisdictions may choose between various options with respect to the local application of QDMTT to Securitisation Entities as set out below:

1. Securitisation Entities shall be within the scope of QDMTT and the QDMTT Safe Harbour shall apply (assuming all other criteria are met);
2. Securitisation Entities shall be within the scope of QDMTT but, where applicable, any QDMTT shall be payable by another entity in the same jurisdiction that is not a Securitisation Entity, and if there is no such entity from which to collect any such QDMTT,
   a. QDMTT shall be payable by the Securitisation Entity, and the QDMTT Safe Harbour shall apply (assuming all other criteria are met); or
   b. QDMTT shall not be payable and, for any group with a Securitisation Entity in the jurisdiction, the Switch-off Rule shall apply (and in this situation there is no entity in the jurisdiction that is not a Securitisation Entity); or
3. Securitisation Entities may be outside the scope of QDMTT and, for any group with a Securitisation Entity in the jurisdiction, the Switch-off Rule shall apply (and in this situation any entity in the jurisdiction in a group that is not a Securitisation Entity, if applicable, is also impacted but credit shall be available for QDMTT paid against any IIR or UTPR, as applicable, in another jurisdiction).

Accordingly, following industry consultation, it is expected that Option 2 above should adopted by Ireland, pending the outcome of any further developments (see below).

UTPR

Jurisdictions also have an option to exclude Securitisation Entities from a liability to top-up taxes under the UTPR, when those rules come into effect in 2025.

Other

The OECD have stated that further work should be carried out on a timely basis so as to ensure that the use of securitisation transactions does not result in top-up taxes payable by groups which is not commensurate with the economic profit of the Securitisation Entity (which should be negligible). Accordingly, further guidance is expected on a timely basis. Specifically, in the preparation of such further guidance it has been indicated that it shall be considered whether a Securitisation Entity should be treated as being deconsolidated from the group for the purposes of the GloBE Rules. If this were the outcome, it would be most welcome, thus excluding Securitisation Entities from the scope of the Pillar 2 GloBE rules entirely.

This document has been prepared by McCann FitzGerald LLP for general guidance only and should not be regarded as a substitute for professional advice. Such advice should always be taken before acting on any of the matters discussed.

Key contacts

Eleanor MacDonagh
Head of Financial Services Tax

Deirdre Barnicle
Partner