Pillar Two with SAP

The introduction of Pillar Two, which intends to implement a worldwide global minimum taxation, already presents a major challenge for multinational companies. Pillar Two is intended to ensure an effective minimum tax rate of 15 % in each country, in which the group operates, provided the group exceed an annual revenue of 750 million euros. If the effective tax rate in a jurisdiction is below 15 %, a Top-up Tax increases the taxation in the affected jurisdiction to 15%. Even if a number of multinational groups currently assume that they will only be affected marginally or not at all by the Top-up Tax, it is the significantly higher compliance requirements that represent a great challenge for multinational groups.

Understanding the complex Pillar Two regulations is a major challenge for the companies, but that is only one aspect of the forthcoming challenges. Above all, they are currently dealing with the development of new processes and guidelines as well as the technical implementation of these processes in order to create the necessary data to be able to comply with the rules in the future. The ongoing correct execution of the Pillar Two rules requires a large amount of information and data to be available within a very short timeframe, in particular during reporting periods where time is already of the essence. This includes data that has not yet been available to the companies in the required form and level of detail but is now required in order to meet the reporting obligations. Therefore, an automation of the data collection process as well as an automation of the subsequent Pillar Two calculation is essential for multinational groups.

In order to ensure the Pillar Two compliance and to meet the reporting requirements, a process for the provisioning of data is inevitable. To achieve this, existing data gaps must be identified and closed and a Pillar Two target data model as well as changes to current accounting processes must be defined. In addition, a solid technical understanding of the Pillar Two rules and the resulting compliance requirements is essential. This is particularly important to set up the company specific applications of the Pillar Two regulations (e.g. scoping) and to update any existing Tax CMS documentation regarding Pillar Two implications. Once this has been completed, tax accounting and reporting processes have to be designed in order to be able to comply with the new rules in the future. As a result, existing guidelines and documentation need to be updated and communicated. Also, the implementation of a software solution has to be initiated which ideally leads to a digitalization of the entire Pillar Two calculation as well as the subsequent tax declaration process.

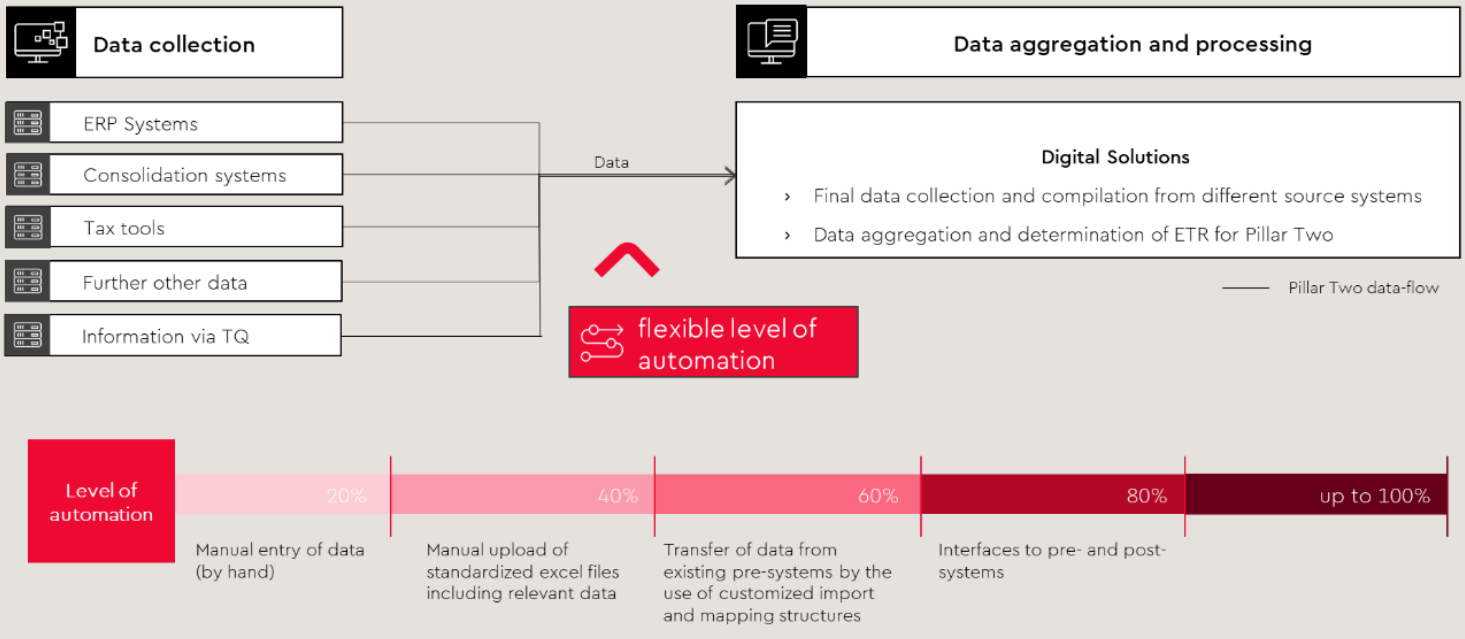
Clearly, to comply with the Pillar Two regulations an increased interdisciplinary collaboration among a wide variety of departments within a multinational group will be required. This collaboration includes not only Accounting, Tax and Digital, but also project and change management, which will be of high importance during the entire Pillar Two compliance project.

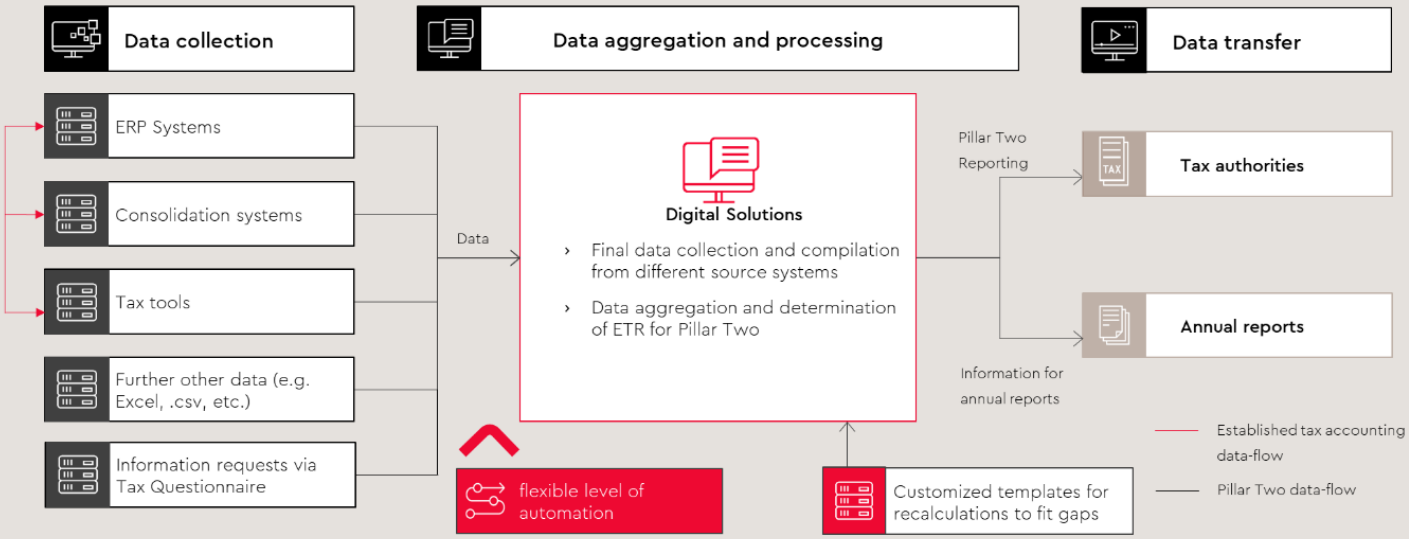
Pillar Two as an accelerator for the digitalization of the (income) tax process

In the past and even today, tax compliance processes, in particular the income tax calculation and the preparation and filing of tax returns, have almost entirely been performed manually. One reason for this is that the necessary data quality and level of detail in most cases is not available and the benefit of an automated process would be relatively low compared to the high implementation and maintenance costs. Furthermore, since taxation regulations (e.g. the treatment of non-deductible expenses or regulations regarding the tax exemption of income) vary from country to country, there has never been an incentive for companies to digitize tax compliance processes because it has not been worth the financial investment to do so. But not only tax regulations and therefore the determination of the taxable income is different in every country. Various data sources and interfaces used for the transmission of tax returns to the respective tax authorities also vary from country to country.

With the introduction of the Pillar Two rules, for the first time there is now a globally uniform taxation system which relies on globally uniform accounting standards (e.g. IFRS). Therefore, collection and processing data manually will no longer be an efficient approach. Due to the increased compliance requirements and limited human resources, companies are left with no other option but to automate the Pillar Two process as much as possible. This is only possible with adequate data management. For the Pillar Two calculations, a large amount of the collected data is required for different countries and can therefore be used multiple times. One particular example for this is the calculation of deferred taxes. In the past, deferred taxes used to be relevant only for the group financial statements. Therefore, the exact correct determination of deferred taxes has never been the highest priority. However, under Pillar Two, the correct calculation of deferred taxes is of the highest importance in order to meet the strict compliance requirements. This provides an incentive for tax departments to automate the determination of deferred taxes since this information will be used for multiple reporting obligations.

As a result, the introduction of Pillar Two could be the starting point for the accelerated digitalization of the income tax process.





The symbiosis of data provisioning and utilization

The data and information required for the Pillar Two calculation and the subsequent Pillar Two declaration come from a wide variety of sources. These include ERP systems, consolidation systems, tax tools as well as information provided via a tax questionnaire. The tax questionnaire ensures the provision of relevant data which is not available in the source systems (e.g. whether there have been any transactions not at arm's length). It should be able to collect data efficiently and process the data automatically. However, the largest portion of information and data (approx. 80%) originate from the ERP and consolidation systems. For this purpose, a large portion of multinational companies worldwide use SAP. Therefore, it is only the most logical conclusion that SAP would also be an appropriate solution to perform the Pillar Two calculation. Highly performant interfaces between SAP as a source system and SAP as a Pillar Two IT solution ensure the transfer of data between affected systems in the most efficient way.

Must-have features of a good Pillar Two IT solution

Since the exact design of the Pillar Two OECD Model rules has only recently been published, the offered IT solutions on the market are still scarce at this time. Products currently on the market include existing tax reporting solutions which have been extended to include Pillar Two as well as entirely new developments. Existing tax reporting solutions offer the advantage that user interfaces are already familiar and existing master and reporting data as well as interfaces can be used efficiently. Newly developed solutions on the other hand offer the advantage of being developed specifically to meet the needs of the company in a practical way. Basically, a good Pillar Two IT solution should meet the following requirements:

High level of flexibility

The Pillar Two IT solution should be able to adapt to the individual data, IT, and process structures of different corporations. Therefore, the tool should be able to operate with various source systems. A high level of flexibility is also necessary as tax regulation adjustments or changes in the group's internal or external environment may occur at any time.

High level of automation

The data import, the data preparation as well as the calculations required for the Pillar Two process should be performed by the tool with as much automation as possible. The user should be able to see, based on the results, if and to what extent a Top-up Tax must be recognized in the financial statements. At the same time, manual adjustments and professional assessments of the data and results should be ensured at all times.

High performance

The Pillar Two IT solution should be able to process large quantities of data in an efficient and flexible manner. In addition to the aggregation of data, this also includes the calculations as well as the possibility of a subsequent data analyzation.

User-friendly interface

The user interface of the Pillar Two IT solution should be intuitive and easy to use. The tool should guide the end user step-by-step and in a straightforward manner throughout the entire calculation process so that the next steps are clear at all times.

Different user perspectives

The Pillar Two IT solution should be able to illustrate different user perspectives so that the different entity and country specific calculations can be performed. Here, at least the role of a preparer who initially performs the calculations should be implemented. In addition, the role of a reviewer should exist to ensure a validation and approval of the results. Ideally, the administration of master data can also be performed within the tool.

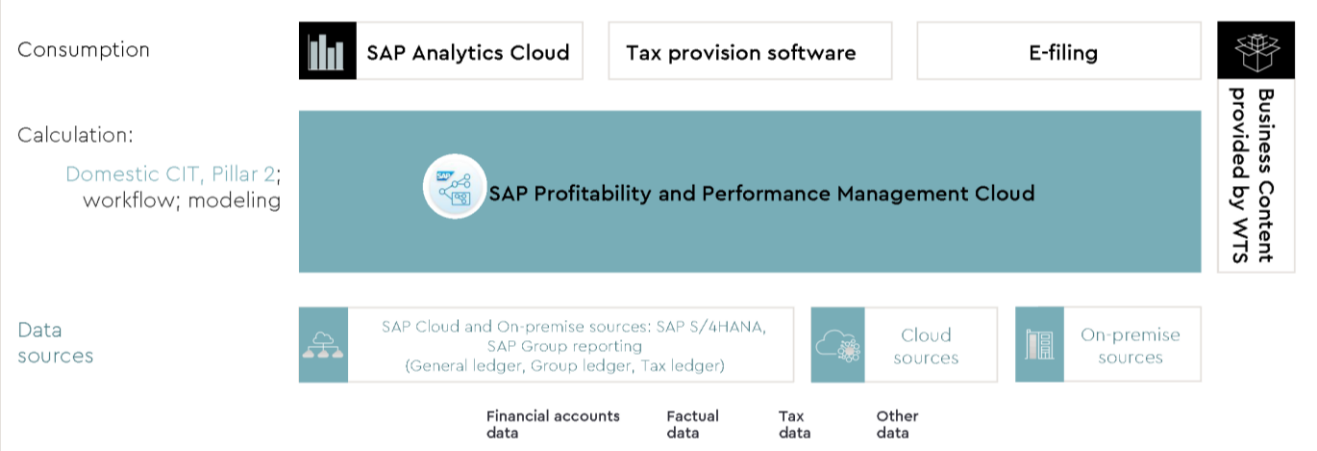
Practice-oriented

Problems and challenges of the „real world" should be considered during the development of the solution so that a practical relevance of the tool is ensured.

SAP architecture for Pillar 2 solution

As BEPS Pillar 2 process goes far beyond Tax department and requires collaboration between various departments SAP offers an end-to-end architecture that allows customers to not only leverage a flexible modeling platform (SAP PAPM) to enable seamless calculation of income tax and BEPS Pillar 2. Moreover, SAP PAPM solution natively integrates with SAP S/4HANA and SAP Group reporting allowing to use the most accurate data coming directly and with no replication from transactional systems. This enables easier, more efficient compliance with tax requirements, eliminate manual reconciliations and enable audit trail with drilldown to transaction details. This architecture allows our customers to create one repository, a single source of truth for the data required to calculate income tax, do simulations, and improve visibility into tax data, this is also a scalable platform for further use cases that can be atomized using SAP PaPM solution e.g., Operational Transfer Pricing.

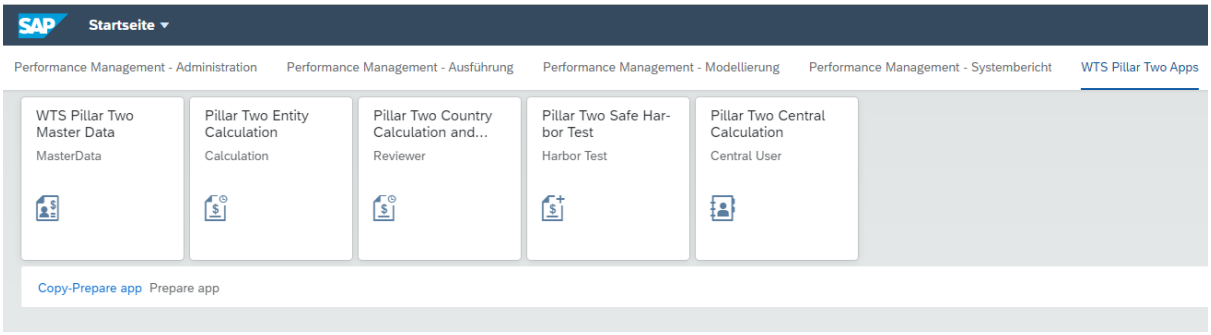
To make these processes of automatization and calculation even more compliant SAP also offers **Tax compliance** and **Process management solutions**.



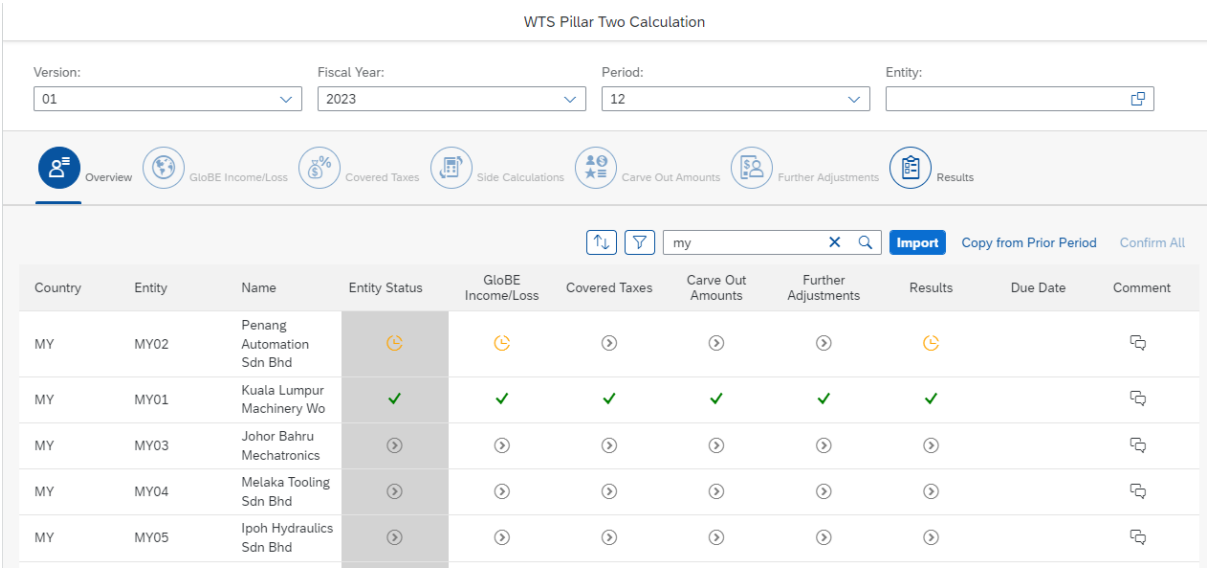
WTS solution based on SAP technology

Over the course of the last year we have been developing a Pillar Two IT solution in SAP Profitability and Performance Management (PaPM) combined with a state of the art SAP Fiori user interface. The development has been carried out in close cooperation with a large German multinational group in order to ensure a most practice-oriented approach. In addition to the development of standard functionalities, PaPM offers the advantage of flexible customization to group specific needs. PaPM is particularly suitable for companies with a broad ERP landscape as it is able to operate with a variety of different source systems (e.g. MS Excel, non-SAP ERP systems as well as multiple consolidation systems).

PaPM acts as a data aggregator, computation engine, simulation software and analysis tool in one. It is able to process large amounts of data efficiently. With our solution in SAP PaPM all Pillar Two requirements will be met. With all apps necessary to perform the relevant Pillar Two calculations in one place, our solution offers an efficient and easy way to tackle the complex Pillar Two requirements - all with a user-friendly interface.



With a comprehensive and guided process, our solution leads the user through the entire calculation process - step-by-step. Thanks to the user-friendly and self-explanatory interface, our solution ensures that during each step the user knows which task to complete next. In addition, an illustrative status tracking is possible at all times.



Enabling different user perspectives, our solution ensures that in addition to the role of an entity preparer who performs the calculations at entity level, there is also a country preparer who performs the required calculations at country level, which is a crucial step of the Pillar Two calculation. Furthermore, the role of a central user has been implemented. The central user is able to view the processing status of all companies and countries and can review and adjust if necessary. In addition, the administration of master data (e.g. scoping, mapping) can also be performed within the tool.

At the push of a button, the data can be imported and processed. However, manual adjustments and entries of comments are also possible at each step of the process. Our solution is able to perform all necessary Pillar Two calculations: from the determination of the GLOBE income, adjusted covered tax and effective tax rate to the calculation of the Top-up Tax and the subsequent allocation of the Top-up Tax between the different jurisdictions - all in accordance with the Pillar Two rules. Furthermore, the calculations according to the Safe Harbour rules have been implemented as well. With the option

to generate various reports, the results can be flexibly integrated into the tax reporting process. Therefore, our solution meets all of the complex Pillar Two compliance requirements.

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