PUBLIC CONSULTATION DOCUMENT

Pillar One – Amount A: Regulated Financial Services Exclusion

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OECD
BETTER POLICIES FOR BETTER LIVES

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Background

Introduction

Following years of intensive negotiations to update and fundamentally reform international tax rules, 137 members of the OECD/G20 Inclusive Framework on BEPS (Inclusive Framework) joined the *Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy* (the Statement) released in October 2021. The Statement sets out the political agreement on the key components of Pillar One and Pillar Two.

Amount A of Pillar One has been developed as part of the solution for addressing the tax challenges arising from the digitalisation of the economy. It introduces a new taxing right over a portion of the profit of large and highly profitable enterprises for jurisdictions in which goods or services are supplied or consumers are located.

The Inclusive Framework has mandated the Task Force on the Digital Economy (TFDE) – a subsidiary body – to advance the work needed to implement Amount A. In particular, the TFDE has been charged with developing the Multilateral Convention (MLC) and its Explanatory Statement as well as the Model Rules for Domestic Legislation (Model Rules) and related Commentary through which Amount A will be implemented.

Model Rules

The Model Rules, once finalised, will reflect the substantive agreement of the members of the Inclusive Framework on the functioning of Amount A and will serve as the basis for the substantive provisions that will be included in the MLC. The Model Rules are also being developed to provide a template that jurisdictions could use as the basis to give effect to the new taxing rights over Amount A in their domestic legislation. They will be supported by a commentary. Jurisdictions will be free to adapt these Model Rules to reflect their own constitutional law, legal systems, and domestic considerations and practices for structure and wording of legislation as required, whilst ensuring implementation is consistent in substance with the agreed technical provisions governing the application of the new taxing rights.

The Model Rules will cover all aspects of Amount A that would be translated into domestic law. They will consist of different titles. This document covers the Schedule of the Model Rules that will govern the Exclusion for Regulated Financial Services.

Model Rules on Regulated Financial Services Exclusion

The Regulated Financial Services Exclusion will exclude from the scope of Amount A the revenues and profits from Regulated Financial Institutions. The defining character of this sector is that it is subject to a unique form of regulation, in the form of capital adequacy requirements, that reflect the risks taken on and borne by the firm. It is this regulatory driver that generally helps to align the location of profits with the market. The scope of the exclusion derives from that requirement, meaning that Entities that are subject to risk-based capital measures (and only those) are excluded from Amount A.

There are six types of Regulated Financial Institution defined in this document: Depositary Institution; Mortgage Institution; Investment Institution; Insurance Institution; Asset Manager; a Mixed Financial Institution. A seventh category is added, for a limited type of service entity that exclusively performs functions for a Regulated Financial Institution (RFI Service Entity).

The definition for each type of Regulated Financial Institution generally contains three elements, all of which must be satisfied: a licensing requirement; a regulatory capital requirement; and an activities requirement. These conditions recognise the uniquely regulated nature of financial services. Where the conditions are met, the revenues and profits of the Entity are wholly excluded from Amount A.

However, commentators should note that this does not reflect the final or consensus views of the Inclusive Framework and that some members hold the view that reinsurance and asset management ought not to be excluded from Amount A.

The schedule for the Regulated Financial Services Exclusion contained in this document provides a description and explanation of the envisaged draft rules. Other than the definitions for the scope of the Regulated Financial Services Exclusion, which are presented in draft Model Rules format, this document is in narrative format. This is because other parts of the Model Rules on Amount A, on which corresponding provisions for the Regulated Financial Services Exclusion would be based, are pending finalisation.

The relevant sections on Scope (currently Title 2), as well as relevant definitions (currently included in Title 9), and which were the subject of an earlier public consultation document released on 4 April 2022 are included in the Annex for context. In addition, explanatory footnotes are included in the document to assist public commentators in reviewing the substantive proposal, and to note where further material is expected to be included in Commentary.

Public consultation instructions

This is a working document released by the OECD Secretariat for the purposes of obtaining input from stakeholders. It does not reflect the final views of the Inclusive Framework members. It presents the work undertaken to date, which has reached a sufficient level of detail and stability allowing it to be suitable for consultation. The TFDE has agreed that this working version can be released on the basis that it is without prejudice to the final agreement. As such, while the document is intended to illustrate the framework for the Regulated Financial Services Exclusion, further changes may be made to the conceptual framework, as well as then being translated into Model Rules format. Thus, the release of this document reflects consensus within the TFDE as a procedural matter that public comments should be sought at this time, but does not reflect consensus within the TFDE regarding the substance of the document.

Comments are sought with respect to the rules described in this document. While comments are invited on any aspect of the rules, input will be most helpful where it explains any areas where the definitions of Regulated Financial Institutions are unclear or insufficient (including the reasonableness of the thresholds proposed); the practical challenges in applying the rules for identifying excluded and in-scope revenues and profits; and the additional guidance or compliance simplifications that would be needed to effectively apply the Regulated Financial Services Exclusion.

Interested parties are invited to send their comments on this discussion draft no later than 20 May 2022. These comments will be examined at the following meeting of the TFDE.

Comments on this discussion draft should be sent electronically (in Word format) by email to tfde@oecd.org and may be addressed to: Tax Treaties, Transfer Pricing and Financial Transactions Division OECD/CTPA.

Please note that all written comments received will be made publicly available on the OECD website. Comments submitted in the name of a collective “grouping” or “coalition”, or by any person submitting comments on behalf of another person or group of persons, should identify all enterprises or individuals who are members of that collective group, or the person(s) on whose behalf the commentator(s) are acting.

Schedule [G]: Regulated Financial Services Exclusion

Overview

1. The Regulated Financial Services Exclusion will exclude from the scope of Amount A the profits from Regulated Financial Institutions. This first section provides an overview of the seven steps that a Group that qualifies for the Regulated Financial Services Exclusion would follow to apply Amount A as a whole. For simplicity, these rules will be contained in a Schedule of the Model Rules, Schedule G. Steps 2 and 3 are specific to the Regulated Financial Services Exclusion, and it is these parts on which public comments are invited.

Application of the Regulated Financial Services Exclusion

2. The Regulated Financial Services Exclusion would be applied taking the following steps:

3. ***Step 1***: Apply the general scope rules. This is the first step which any Group will apply to assess whether it falls in scope of Amount A. This means that a Group will only be potentially in-scope of Amount A where either the Group on a consolidated basis (including activities covered by the exclusion), or a disclosed segment (where the exceptional segmentation rules apply), has more than EUR 20 billion of revenue[1] and a profit margin above 10%. In applying the general Amount A scope provisions, the Group would also need to take into account the effect of *the average test* and *the prior period test* (see public consultation document on these scope rules released on 4 April 2022 and relevant provisions of this document contained in the Annex). If the Group (and any disclosed segment, if applicable) does not meet both of these scope thresholds, it is not in scope of Amount A and need not continue. Only if the Group (or disclosed segment, where applicable) has more than EUR 20 billion of revenue, and a profit margin above 10% (including under the average test and prior period test) does it then continue to step 2.

4. ***Step 2***: Re-determine whether the EUR 20 billion revenue threshold is met, by testing only the in-scope (i.e. non-Regulated Financial Services) revenue. This means excluding the revenue from Regulated Financial Services at the level that the taxpayer is found to be in-scope under step 1 (i.e. either at the level of the Group or the level of a disclosed segment). If the remaining in-scope revenues are not above EUR 20 billion, the Group (or disclosed segment, where the exceptional segmentation rules apply) is not in scope. If it is above EUR 20 billion, continue to step 3.

[1] As outlined in the Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy the Amount A revenue threshold will be: “reduced to 10 billion euros, contingent on successful implementation including of tax certainty on Amount A, with the relevant review beginning 7 years after the agreement comes into force, and the review being completed in no more than one year.” In this document, the EUR 20 billion threshold is used, without prejudice to this part of the Statement.

5. ***Step 3***: Re-determine whether the 10% profitability threshold is met, by isolating the Regulated Financial Services profits, and testing the profit margin of the remaining in-scope profits against in-scope revenues. Again, this exercise is undertaken by excluding the Regulated Financial Services at the level that the taxpayer is found to be in-scope under step 1 (i.e. either at the level of the Group or the level of a disclosed segment). If this profit margin is below 10%, the Group (or disclosed segment, where the exceptional segmentation rules apply) is out of scope. If it is above 10%, continue to step 4. Work is ongoing in considering how the application of the Regulated Financial Services Exclusion can be simplified, particularly for Groups that exceed the revenue threshold, but whose in-scope profit margin is consistently below the 10% profitability threshold.

6. ***Step 4***: Apply the rules for nexus and revenue sourcing. The nexus threshold will only be met where the in-scope revenues sourced to a jurisdiction exceed the agreed nexus revenue threshold. Revenues covered by the Regulated Financial Services Exclusion shall not be taken into account for the purpose of applying the nexus test. The general Amount A revenue sourcing rules will apply to the in-scope revenue of a Group (or disclosed segment) that is not covered by the Regulated Financial Services Exclusion.

7. ***Step 5***: Apply the rules for the determination and allocation of taxable profit to a Jurisdiction for a Period.[2] This will be the same as the ordinary profit allocation formula that applies for Amount A. The profits that are covered by the Regulated Financial Services Exclusion will not be taken into account for the purposes of applying the Marketing and Distribution Profits Safe Harbour.

8. ***Step 6***: The mechanism to eliminate double taxation will not result in the profits that are covered by the Regulated Financial Services Exclusion being used to eliminate double taxation arising from Amount A. These profits will be excluded from the mechanism to eliminate double taxation.

9. ***Step 7***: File the necessary documentation for the purposes of administration and reporting. Documentation requirements will be set out in the relevant provisions on administration. The process for filing this documentation as part of the tax certainty process will be set out in the relevant provisions on tax certainty.

10. Steps 2 and 3, which are the operative provisions specific to the Regulated Financial Services Exclusion, are discussed in further detail below.

Step 2: Identify Regulated Financial Services Activities and apply the Revenue Threshold to in-scope revenue

11. The revenue threshold for Amount A is designed to apply to consolidated group revenue, and it has been set at EUR 20 billion (as applied at Step 1). In exceptional circumstances, a disclosed segment may fall in-scope under step 1 (where the segment meets the revenue and profitability threshold, but the Group does not meet the latter). The purpose of Step 2 is to re-apply the revenue threshold at the level of the Group or disclosed segment (whichever fell in-scope under step 1), but only looking at the in-scope revenue.

12. This test is applied by taking the consolidated Group revenue figure,[3] and subtracting third party revenue derived from Regulated Financial Services. As defined in Title 9, Regulated Financial Services,

[2] The term Period is defined in the Model Rules. It means a reporting period with respect to which the Ultimate Parent Entity of a Group prepares Consolidated Financial Statements.

[3] Or the revenue of a disclosed segment, if the exceptional segmentation rules are the basis on which the Group met the scope threshold in Step 1.

means services carried out by a Regulated Financial Institution as defined in Schedule [G]. This means that the exclusion is operated on an Entity-by-Entity basis. An Entity that meets the definition of Regulated Financial Institution is wholly excluded from Amount A. An Entity that does not meet that definition is wholly included in Amount A. An Entity, for the purposes of Amount A, includes any branches, whether or not there is a permanent establishment under domestic law and the applicable tax treaty, and the Entity is tested as a whole.[4]

13. This test is applied as follows. The taxpayer identifies the Regulated Financial Institutions that meet the definitions below. Only the revenue of the remaining entities in the Group is tested to determine whether it exceeds EUR 20 billion. This is done by adding the third party revenues of each non-excluded Entity.

14. However, as a matter of practice to reduce the compliance burden of administering step 2, a taxpayer may apply this test in a simplified manner, in two ways.

- The taxpayer could identify its largest Regulated Financial Institutions, and subtract the total third party revenues of such entities from the consolidated revenue figure (or the revenues at the level of the disclosed segment, if relevant). It does not need to identify and remove every Regulated Financial Institution; it would be sufficient to remove the revenue of Regulated Financial Institutions to the extent that the remaining revenue is below EUR 20 billion. In other words, the taxpayer is not required to apply the exclusion to the fullest extent, but only insofar as it is necessary to establish that the remaining revenue does not exceed EUR 20 billion and therefore the Group or disclosed is not in scope.
- An additional simplification, which a taxpayer could apply as an alternative to subtracting third party revenues from the consolidated revenues (or disclosed segment revenues), is testing whether the revenues of the remaining in-scope Entities exceed EUR 20 billion by adding the total revenues of all such Entities. This would mean the taxpayer does not need to further subtract the intra-group revenue. This is a practical approach which means the taxpayer will over-include revenue for this test. If the total such revenues of in-scope Entities are still below EUR 20 billion, then the Group (or disclosed segment) is not in scope, even though it has not applied the benefit of the excluded revenue test to the fullest extent that it was entitled to.

15. It is anticipated that this part of the test will be relevant for most, if not all, financial services Groups, which are likely to have limited amounts of third party revenue earned outside the Regulated Financial Institutions. As such it is intended to provide a filtering function using a rule that is relatively easy to apply and document, and to be reviewed by tax administrations.

16. The test would use the following definitions:

Title 9 – Definitions

17. “Revenues” of a Group for a Period means the Total Revenues of the Group for the Period after the exclusion of revenues derived from Extractive Activities and Regulated Financial Services.

[4] The term “Entity” is defined in the Model Rules. “Entity” means any legal person (other than a natural person) or an arrangement, including but not limited to a partnership or trust, that prepares, or is required to prepare, separate financial accounts.

18. “Regulated Financial Services” means services carried out by a Regulated Financial Institution as defined in Schedule [G].[5]

Schedule G – Regulated Financial Services Exclusion

19. “Regulated Financial Institution” means a Depositary Institution; Mortgage Institution; Investment Institution; Insurance Institution; Asset Manager; a Mixed Financial Institution; and an RFI Service Entity.[6]

20. “Depositary Institution” means a Group Entity:[7]

a. That is licensed to carry on the activity listed in paragraph (c) as a bank under the laws or regulations of the jurisdiction in which the Group Entity does that business[8] or, in the case of a Group Entity that does such business in a European Economic Area (EEA) Member State, is licensed by a competent authority to carry on such business in an EEA Member State; and

[5] The Commentary would explain that the term “Regulated” is specific to financial services, rather than a general concept that there is government oversight or consumer protection (which applies to a range of other sectors). It focusses on prudential requirements based on capital adequacy.

The elements of the definitions concerning regulation for the purposes of the exclusion from Amount A are intentionally high level and principles-based. It recognises that there are broadly accepted international approaches to capital adequacy requirements, in the case of banking in particular, that can serve as a common framework for the exclusion. A similar basic principle is drawn upon in defining the “regulated” requirement in respect of each Regulated Financial Institution, which recognise that the determination of the amount of capital required to be held must take into account the risks taken on and presented by the Entity. At the same time, the requirement does not require a technical examination of every domestic regulatory regime, recognising that domestic regulators may adopt different approaches at a granular level to prescribing capital adequacy requirements, to take account of the varied levels of complexity and risks posed by financial services businesses in different national contexts. This also recognises that it would in any event not be feasible for the Inclusive Framework to define, or the tax certainty panel to verify, whether the particular type and quality of regulation imposed by a local regulator is in line with these international approaches. That is the mandate and area of competence of other bodies, such as the Basel Committee on Banking Supervision.

The test for regulation applies at an Entity level, meaning that the effect of the regulation is that it either requires a separate, appropriately capitalised entity to be established for operating within a market, or it requires local branches of foreign entities to be able to call on sufficient capital of the entity or capital held in the local branch. In other words, the rules do not require that the entity is subject to capital adequacy requirements in each branch location, but instead require that the entity (as a whole) is subject to regulation by the home state regulator.

[6] As noted in the Background, commentators should note that this does not reflect the final or consensus views of the Inclusive Framework and that some members hold the view that reinsurance and asset management ought not to be excluded from Amount A.

[7] The term Group Entity means any Entity, other than an Excluded Entity, whose assets, liabilities, income, expenses and cash flows are, or would be, included in the Consolidated Financial Statements of a UPE. This term is used to ensure that it does not include an Excluded Entity (which is defined as a Governmental Entity, an International Organisation, a Non-profit Organisation, a Pension Fund, an Investment Fund or a Real Estate Investment Vehicle). This means that the definition of Excluded Entity is applied in priority to the exclusion for Regulated Financial Services.

[8] The Commentary would explain that this licensing requirement is tested looking at the operations in the local jurisdiction, and may need to be tested at branch rather than Entity level. The reference to being licensed to carry on business under the laws or regulations of the jurisdiction in which the Group Entity does that business also includes cases where that laws or regulations of that Jurisdiction provide for the recognition of the licensing decision of another Jurisdiction, for example, under equivalence regimes. This Commentary also applies to the same licensing test as applies under sub-paragraph (a) of the other definitions of Regulated Financial Institution.

b. That is subject to capital adequacy requirements that reflect the Core Principles for Effective Banking Supervision as provided by the Basel Committee on Banking Supervision; and

c. That accepts Deposits in the ordinary course of a banking or similar business;[9] and

d. For which at least [20] percent of the liabilities of the Entity consist of Deposits, as at the balance sheet date for the Period

but does not include a Group Entity a substantial portion of whose business is to accept or manage funds from, and provide associated services to, Group Entities of the same Group that are not Regulated Financial Institutions.[10]

21. "Mortgage Institution" means a Group Entity:

a. That is licensed to carry on the activities listed in paragraph (c) under the laws or regulations of the jurisdiction in which the Group Entity does that business or, in the case of a Group Entity that does such business in a European Economic Area (EEA) Member State, is licensed by a competent authority to carry on such business in an EEA Member State; and

b. That is subject to capital adequacy requirements that reflect the Core Principles for Effective Banking Supervision as provided by the Basel Committee on Banking Supervision; and

[9] The Commentary would explain that an Entity is considered to be engaged in a "banking or similar business" if, in the ordinary course of its business with customers, the Entity accepts Deposits and regularly engages in one or more of the following activities:

a) makes personal, mortgage, industrial, or other loans or provides other extensions of credit;

b) purchases, sells, discounts, or negotiates accounts receivable, instalment obligations, notes, drafts, checks, bills of exchange, acceptances, or other evidences of indebtedness;

c) issues letters of credit and negotiates drafts drawn thereunder;

d) provides trust or fiduciary services;

e) finances foreign exchange transactions;

f) enters into, purchases, or disposes of finance leases or leased assets.

An Entity is not considered to be engaged in a banking or similar business if the Entity solely accepts deposits from persons as a collateral or security pursuant to a sale or lease of property or pursuant to a similar financing arrangement between such Entity and the person holding the deposit with the Entity.

[10] The Commentary would explain that the effect of this sub-paragraph is to ensure that Entities such as group treasury centres do not qualify for the Regulated Financial Service exclusion. In this context, a "substantial portion" means that total gross income attributable to the holding of funds from Group Entities in the same Group and associated services (such as managing liquidity, foreign exchange risk, intra-group payment processes, financial governance and risk management, and related analytics) equals or exceeds [50] per cent of the Group Entity's total gross income during the Period. However, it does not prevent the exclusion from applying where an Entity otherwise meets the definition and provides the activities listed in paragraph (c) to other Regulated Financial Institutions in the same Group.

c. That accepts repayable funds[11] from the public for the purpose of granting credits for its own account in the ordinary course of a banking or similar business[12] provided the credits are granted directly to individuals for the purchase of real estate (or refinancing of such prior credits) and it receives security for the repayment of those credits in the form of mortgages and

d. For which the total gross income[13] attributable to the granting of such credits equals or exceeds [75] per cent of the Group Entity's total gross income during the Period

but does not include a Group Entity a substantial portion of whose business is to provide credits to Group Entities of the same Group that are not Regulated Financial Institutions, or to provide credit for the purchase of the Covered Group's own goods.[14]

22. "Investment Institution" means a Group Entity:[15]

a. That is licensed to carry on the activities listed in paragraph (c) as a business under the laws or regulations of the jurisdiction in which the Group Entity does that business or, in the case of a Group Entity that does such business in an EEA Member State, is licensed by a competent authority to carry on such business in an EEA Member State; and

b. That is subject to capital adequacy requirements that reflect the Core Principles for Effective Banking Supervision as provided by the Basel Committee on Banking Supervision or Objectives and Principles of Securities Regulation as adopted by the International Organisation of Securities Commissions (IOSCO) and the related implementing methodology; and

c. For which the total gross income attributable to one or more of the following activities equals or exceeds [75] per cent of the Group Entity's total gross income during the Period:

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[11] The Commentary would explain that the term "repayable funds" means funds that are the subject of a contractual agreement to repay the funds, and includes bonds and other comparable securities such as negotiable certificates of deposits, provided that these are continually issued by the credit institution (and not as a one-off or occasional form of capital-raising). The phrase "from the public" means from any persons other than the Mortgage Institution or Group Entities in the same Group. It would also explain that this condition (c) requires that the Entity both accept such repayable funds as well as, and specifically for the purpose of, providing mortgages for its own account.

[12] See footnote 9.

[13] The Commentary would explain that the term gross income means the same as revenue; but the term gross revenue is used to avoid confusion with the defined term "Revenue" in Amount A, which broadly means total revenue minus excluded revenue, and which would create a circular meaning in this contexts of defining the exclusion. Also used in the definition of Investment Institution, Insurance Institution and Asset Manager.

[14] The Commentary would explain that that the effect of this sub-paragraph is to ensure that Entities such as group treasury centres do not qualify for the Regulated Financial Service exclusion, nor do entities that are providing loans for the purchase of the group's own goods. In this context, a "substantial portion" means that total gross income attributable to the holding of funds from, and provision of credit to, Group Entities in the same Group equals or exceeds [50] per cent of the Group Entity's total gross income during the Period. However, it does not prevent the exclusion from applying where an Entity otherwise meets the definition and provides the activities listed in paragraph (c) to other Regulated Financial Institutions in the same Group.

[15] The Commentary would explain that this is a generic term, intended to capture what may be called a custodial institution, investment bank, investment firm, or broker / dealer.

i. dealing, broking or trading in Financial Assets for own account or for account of customers; and / or
ii. holding securities in inventory; and / or
iii. hedging customer transactions; and / or
iv. participating in underwriting, mergers and acquisitions, syndication, securitisation and securities issues and providing financial services related to such activities;[16] and / or
v. holding, transferring, controlling, administering or distributing Financial Assets for the account of other persons;

but does not include a Group Entity a substantial portion of whose business is to manage investments of Group Entities of the same Group that are not Regulated Financial Institutions.[17]

23. “Insurance Institution” means a Group Entity:

a. That is licensed to carry on the activities listed in paragraph (c) as a business under the laws or regulations of the jurisdiction in which the Group Entity does that business or, in the case of a Group Entity that does such business in an EEA Member State, is licensed by a competent authority to carry on such business in an EEA Member State; and

b. That is subject to solvency standards incorporating a risk-based capital measure; and

c. The gross income of which arising from Insurance Contracts and Annuity Contracts (including investment income from assets associated with such contracts) for the Period exceeds [75] per cent of total gross income for such Period; or the aggregate value of the assets held to manage risk associated with Insurance Contracts and Annuity Contracts exceeds [75] per cent of total assets as at the balance sheet data for the Period;

but does not include a Group Entity a substantial portion of whose insurance business is to provide Insurance Contracts to Group Entities of the same Group or to reinsure policies covering risks of Group Entities of the same Group, that are not Regulated Financial Institutions.[18]

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[16] The Commentary would explain that this includes: granting credits or loans to an investor to allow them to carry out a transaction in one or more financial instruments where the firm granting the credit or loan is involved in the transaction; advice to undertakings on capital structure, industrial strategy and related matters; advice and services relating to mergers, restructuring, the purchase or disposal of undertakings; investment research and financial analysis or other forms of general recommendation relating to transactions in financial instruments; and services related to underwriting.

[17] The Commentary would explain that that the effect of this sub-paragraph is to ensure that Entities such as group treasury centres do not qualify for the Regulated Financial Service exclusion. In this context, a “substantial portion” means that total gross income attributable to providing investment services to Group Entities in the same Group equals or exceeds [50] per cent of the Group Entity’s total gross income during the Period. However, it does not prevent the exclusion from applying where an Entity otherwise meets the definition and provides the activities listed in paragraph (c) to other Regulated Financial Institutions in the same Group.

[18] The Commentary would explain that that the effect of this sub-paragraph is to ensure that Entities such as captive insurers do not qualify for the Regulated Financial Service exclusion. In this context, a “substantial portion” means that total gross income attributable to the Insurance Contracts and Annuity Contracts written, or the aggregate value of the assets held to manage risk associated with Insurance Contracts and Annuity Contracts written, for Group Entities in the same Group equals or exceeds [50] per cent of the Group Entity’s total gross income during the Period. However,

24. “Asset Manager” means a Group Entity:

a. That is licensed to carry on the activities listed in paragraph (c) as a business under the law or regulations of the jurisdiction in which the Group Entity does that business, or in the case of a Group Entity that does such business in an EEA Member State, is licensed by a competent authority to carry on such business in an EEA Member State; and

b. That is subject to capital adequacy requirements incorporating a risk-based measure;[19]

c. For which the total gross income attributable to one or more of the following activities equals or exceeds [75] per cent of the Group Entity’s total gross income during the Period: investing in, administering, managing or distributing interests in, an Investment Fund or Real Estate Investment Vehicle, Financial Assets, or money for or on behalf of other persons;[20]

but does not include a Group Entity a substantial portion of whose business is to manage investments of Group Entities of the same Group that are not Regulated Financial Institutions.[21]

25. “Mixed Financial Institution” means a Group Entity:

a. That is licensed to carry on business as described in paragraph (a) of any of the definitions of Depositary Institution, Investment Institution, Insurance Institution, or Asset Manager; and

b. That is subject to requirements to hold a minimum level of capital as described in paragraph (b) of that definition; and

c. For which the total gross income attributable to any of the activities described in paragraph (c) of the definitions of Investment Institution, Insurance Institution, or

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it does not prevent the exclusion from applying where an Entity otherwise meets the definition and provides the activities listed in paragraph (c) to other Regulated Financial Institutions in the same Group.

[19] The Commentary would explain that this requires that the determination of the amount of capital to be held takes into account an entity’s risks. The risks that could be considered in this assessment include assets under management, size, liabilities, execution volumes, credit risk, market risk, or operational risk. This requirement would therefore not be met in Jurisdictions that impose a fixed minimum amount of capital for all firms, without any variation according to the facts and circumstances of individual entities.

[20] The Commentary would explain that the assets listed in this paragraph are intended to be expansive, and include traditional portfolio investments such as those held by collective investment vehicles, as well as alternative asset classes such as infrastructure or controlling interests in other companies. This is achieved by the reference to Investment Fund or Real Estate Investment Vehicle, which are defined broadly under the Model Rules. The reference to “for or on behalf of other persons” means that it includes both the management of investments for an investor, as well as the management of investments for a third party, such as the management of segregated accounts or pension plans on behalf of clients.

[21] The Commentary would explain that that the effect of this sub-paragraph is to ensure that Entities such as group treasury centres do not qualify for the Regulated Financial Service exclusion. In this context, a “substantial portion” means that total gross income attributable to providing investment services to Group Entities in the same Group equals or exceeds [50] per cent of the Group Entity’s total gross income during the Period. However, it does not prevent the exclusion from applying where an Entity otherwise meets the definition and provides the activities listed in paragraph (c) to other Regulated Financial Institutions in the same Group.

Asset Manager equals or exceeds [75] per cent of the Group Entity's total gross income during the Period;

but does not include a Group Entity a substantial portion of whose business is to perform such activities for Group Entities of the same Group that are not Regulated Financial Institutions.[22]

26. "RFI Service Entity" means a Group Entity that:

a. is wholly owned (directly or indirectly) by a UPE of a Group that also wholly owns (directly or indirectly) another Regulated Financial Institution (other than an RFI Service Entity) that is a Group Entity of the same Group; and

b. performs services exclusively for the benefit of one or more other Regulated Financial Institutions (other than an RFI Service Entity) that is a Group Entity of the same Group; and

c. those services are necessary to the carrying out of the activities of such Regulated Financial Institution.[23]

27. "Deposit" means funds which are required to be repaid on demand or at the time agreed under the applicable legal and contractual conditions, with or without interest or a premium. It does not include bonds. It does not include down-payments made by customers as part-payment of the purchase of a good; funds where the principal is not repayable at par or the principal is only repayable at par under a particular guarantee or agreement provided by the financial institution or a third party; payment made by way of security for the performance of a contract or in respect of loss; or payments made by customers in connection with money transfer services.

28. "Financial Assets" includes:

- a money market instrument,
- a security (for example, a share of stock in a corporation; partnership or beneficial ownership interest in a widely held or publicly traded partnership or trust; note, bond, debenture, or other debt instrument),
- a commodity,
- foreign exchange,
- a swap (for example, interest rate swaps, currency swaps, basis swaps, interest rate caps, interest rate floors, commodity swaps, equity swaps, equity index swaps, and similar agreements),

[22] The Commentary would explain that that the effect of this sub-paragraph is to ensure that Entities such as group treasury centres or captive insurers do not qualify for the Regulated Financial Service exclusion. In this context, a "substantial portion" means that total gross income attributable to providing the relevant services referred to in paragraph (c) to Group Entities in the same Group equals or exceeds [50] per cent of the Group Entity's total gross income during the Period. However, it does not prevent the exclusion from applying where an Entity otherwise meets the definition and provides the activities listed in paragraph (c) to other Regulated Financial Institutions in the same Group.

[23] The Commentary would give examples of services that are necessary to the carrying out of the activities of the other Regulated Financial Institutions. This is a narrow category, focussing on administrative services that would typically be remunerated on a cost-plus basis, such as providing payroll functions for employees that perform services solely for the Regulated Financial Institution, holding real estate that is invested in or used by the Regulated Financial Institution as part of its business, and performing other back office and procurement functions for the sole benefit of the Regulated Financial Institution. It would not include the conduct of customer-facing activities, and nor would it cover activities that are not otherwise included in sub-paragraph (c) of the definitions of the other Regulated Financial Institutions above (for example, it would not cover the provision of fintech or payment processing services).

- an Insurance Contract or Annuity Contract,
- interest rate, exchange and index instruments and derivatives,
- any interest (by way of a futures contract, forward contract, option, financial contract for difference or other derivative instrument) in a security, widely held or publicly traded partnership interest, commodity, swap, Insurance Contract, or Annuity Contract.
- However, the term “Financial Asset” does not include a non-debt, direct interest in real property; or a commodity that is a physical good, such as wheat.[24]

29. “Insurance Contract” means a contract of insurance or reinsurance (other than an Annuity Contract) under which the issuer agrees to pay an amount upon the occurrence of a specified contingency involving mortality, morbidity, accident, liability, or property loss risk. It also includes a contract under which a participant agrees to contribute to a common fund providing for mutual financial benefits payable to the participants or their beneficiaries upon the occurrence of a specified contingency involving mortality, morbidity, accident, liability, or property loss risk.

30. “Annuity Contract” means a contract under which the issuer or operator agrees to make payments for a period of time determined in whole or in part by reference to the life expectancy of one or more individuals. The term also includes a contract that is considered to be an Annuity Contract in accordance with the law, regulation, or practice of the jurisdiction in which the contract was issued, and under which the issuer agrees to make payments for a term of years.

Step 3: Identifying excluded and in-scope profits

31. Where a Group (or disclosed segment) meets the general scope provisions in Step 1, and also has more than EUR 20 billion of in-scope third party revenues after the application of Step 2, the taxpayer will need to identify the profits derived from Regulated Financial Services Activities and exclude these from Amount A. The next stage is to identify the remaining profits from in-scope activities to test whether these profits surpass the profitability threshold of 10%.

32. This is a more complex part of the Regulated Financial Services Exclusion. The step is necessary to accurately identify the profits and profitability of non-Regulated Financial Services Activities. The intention is to effectively treat the in-scope part of the Group (or disclosed segment) as a standalone business from the Regulated Financial Services part of the Group. Once the in-scope profits are identified, the profitability test is re-applied.

Identification of in-scope profits

33. Similar to step 2, the calculation to exclude out of scope profits is performed on an Entity-by-Entity basis. This is necessary to be able to accurately apply the definitions, which turn on the presence of the relevant capital adequacy regulation.

34. The taxpayer must identify every in-scope Entity in the Group. This will involve identifying any in-scope entities which were not already identified under step 2 (i.e. because the simplified approach was used to apply the revenue threshold).

[24] The Commentary would explain that the exclusion of a commodity that is a physical good, such as wheat means that a Financial Asset does not include situations where physical delivery of the underlying commodity is taken. Futures contracts and derivatives relating to commodities are including in the meaning of Financial Asset.

35. The taxpayer would then combine the in-scope entities into one consolidated bespoke segment for Amount A purposes. Effectively, this is a notional and bespoke segment for Amount A purposes which includes the non-excluded revenues and profits of the Group or disclosed segment.

36. One way of performing this is a “top-down” approach, which is to undertake the following steps:

- First, exclude or “back-out” the third party revenues and third party costs of Regulated Financial Institutions from the consolidated group or disclosed segment financials.
- Second, include the related-party revenues or related-party costs arising at the level of non-excluded entities (i.e. the bespoke segment) derived from transactions with the Regulated Financial Institutions (that were excluded under the previous bullet).

37. Another way of performing this is to use a “bottom-up” approach, which is to recombine the in-scope entities into a consolidated bespoke segment. This would mean following the segment accounting and / or management accounting principles that would have applied had it decided to publish the entities that do not qualify as a Regulated Financial Institution as one combined disclosed operating segment. This means recognising third party transactions of the in-scope entities, and recognising transactions with the Regulated Financial Institutions in the same Group, but not including revenue earned and costs incurred in relation to transactions between the in-scope entities which are eliminated when preparing the bespoke segment.

38. Whichever approach is used, the principle is that the bespoke segment that is made up of the non-excluded entities of the Group or disclosed segment is treated as a separate and independent business from the Regulated Financial Institutions (meaning that revenue earned and costs incurred from transactions with such Entities is recognised (based on arms’ length principles) rather than eliminated).

39. The Group would make the relevant tax base adjustments as agreed in the rules for calculating the tax base. The resulting Adjusted Profit Before Tax amount is used as the numerator in the profit margin calculation. The denominator is the in-scope revenue amount.

Reapplication of the profitability test

40. The Group would then reapply the profitability test to the new combined consolidated bespoke segment. It would not be subject to Amount A where the profit margin of that bespoke segment is below 10%.

41. If after the reapplication of the threshold profitability test, the in-scope profit margin is above 10%, the average test and profitability test would apply to the bespoke in-scope segment consisting of in-scope entities. However, it is recognised that the bespoke segments would only be created for the purposes of Amount A, and further thought is being given as to how to apply the average test and profitability test in the first years of the application of Amount A.

42. Similarly, a Group would also calculate and carry forward losses relating to its disclosed operating segments / bespoke in-scope segment consisting of in-scope entities. The calculation of historic losses would be calculated in the same way as the calculation of profits described above, that is, in line with accounting principles; but again, recognising the particular challenge of applying these rules in the context of bespoke segments, further consideration is being given as to how to apply this rule.

43. If after the application of the averaging mechanism and losses to the in-scope segment / disclosed operated segment, the profit margin is above 10%, those remaining profits are in scope of Amount A.

Annex: Scope Rules and Definition of Revenue

Title 2: Scope

Article 1: Covered Group

1. The obligations contained in Titles 3 to 9 of this Act apply to any Group Entity of a Covered Group with respect to a Period [beginning][or][ending] on or after the Commencement Date.

2. A Group is a "Covered Group" for a Period where both sub-paragraphs (a) and (b) are met:

   a. The Total Revenues of the Group for the Period are greater than EUR 20 billion (*the global revenue test*). Where the Period is shorter or longer than twelve months, the EUR 20 billion amount is adjusted proportionally to correspond with the length of the Period.

   b. The Pre-Tax Profit Margin of the Group is greater than 10 per cent (*the profitability test*):

      i. in the Period (*the period test*);

      ii. in two or more of the four Periods immediately preceding the Period (*the prior period test*); and

      iii. on Average across the Period and the four Periods immediately preceding the Period (*the average test*).

3. For the purpose of sub-paragraphs (b)(ii) and (b)(iii) of paragraph 2:

   a. where a Group Merger occurs in the Period or any of the three Periods immediately preceding the Period (the "Merger Period") the calculation of the Pre-Tax Profit Margin for the Period(s) prior to the Merger Period should be made by replacing "Group" in that definition with "Acquiring Group", except where there is no "Acquiring Group" in which case "Group" is replaced with "Existing Group"; and

   b. where a Group Demerger occurs in the Period or any of the three Periods immediately preceding the Period (the "Demerger Period") the calculation of the Pre-Tax Profit Margin for the Period(s) prior to the Demerger Period should be made by replacing "Group" in that definition with "Demerging Group".

4. Where a Group meets the conditions in sub-paragraphs (a) and (b) of paragraph 2 and conducts Extractive Activities or Regulated Financial Services, the Group is a Covered Group only if it meets the non-excluded global revenue test and non-excluded profitability test contained in Schedules [F] (*Exclusion of Revenues and Profits from Extractives*) and [G] (*Exclusion of Revenues and Profits from Regulated Financial Services*) of this Act, whichever applies, and any Group Entity of such

Covered Group is subject to the obligations contained in Schedules [F] and [G], whichever applies.

Title 9: Definitions

“Revenues” of a Group for a Period means the Total Revenues of the Group for the Period after the exclusion of revenues derived from Extractive Activities and Regulated Financial Services.

“Total Revenues” of a Group for a Period means the revenues reported in the Consolidated Financial Statements of the Group for the Period prepared in accordance with a Qualifying Financial Accounting Standard, subject to the following adjustments:

a. exclude revenue of the Group for the Period derived from items in Article 5(2)(a)(ii) (Dividends) and Article 5(2)(a)(iii) (Equity Gain or Loss);

b. exclude revenue for the Period derived from an Excluded Entity;

c. adjust for any Eligible Restatement Adjustment of the Group for the Period in accordance with Article 5(2)(b) in instances where the Eligible Restatement Adjustment of the Group for the Period relates to amount(s) that are classified as revenue under a Qualifying Financial Accounting Standard; and

d. adjust for revenue of the Group for the Period to align with the Group’s proportionate share of profit or loss derived from items under paragraph [x] of Title 9 (Joint Venture).

“Regulated Financial Services” means services carried out by a Regulated Financial Institution as defined in Schedule [G].

“Group Entity” means any Entity, other than an Excluded Entity, whose assets, liabilities, income, expenses and cash flows are, our would be, included in the Consolidated Financial Statements of a UPE.