

## Pillar Two Technical Update: Key Changes to GloBE Reporting **Tax Specialty: Washington National Tax Office**

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# Agenda

1. Overview of SbS Package
2. Substance-Based Tax Incentive (SBTI) Safe Harbor
3. Extension of the Transitional CbCR Safe Harbor (TCSH)
4. Simplified ETR Safe Harbor (SESH)



# Meet Today's Presenters



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# 01

## Overview



# Overview: OECD Side-by-Side (SbS) Package



The OECD’s Side-by-Side (SbS) package is designed to simplify the Global Minimum Tax (GMT) contained in the Global Anti-Base Erosion (GloBE) rules (“Pillar Two”).

The SbS package includes a Substance-Based Tax Incentive (SBTI) Safe Harbor that allows multinational enterprise groups (MNE Groups) to benefit from certain tax incentives (e.g., U.S. research and development credit (R&D credit)) that are strongly connected to economic substance in the jurisdiction. In addition to the SBTI Safe Harbor, the SbS package includes a Simplified ETR Safe Harbor as well as extends the Transitional CbCR Safe Harbor.

# 02

## Substance-Based Tax Incentive (SBTI) Safe Harbor



# Overview: Substance-Based Tax Incentive



The SBTI allows MNE Groups to add Qualified Tax Incentives (QTIs) to Adjusted Covered Taxes for entities in a jurisdiction, potentially reducing or eliminating the top-up tax. This addition is limited by a Substance Cap based on payroll and tangible assets in that jurisdiction. MNE Groups can make the SBTI safe harbor election for Fiscal Years beginning on or after January 1, 2026.

**Implications:** The SBTI Safe Harbor comes in direct response to certain concerns shared by the U.S. Department of Treasury during discussions regarding the SbS package which related to the potential treatment of the U.S. R&D credit as a Non-QRTC under Article 4 of the GloBE Rules. Once adopted by Pillar 2 implementing jurisdictions, MNE Groups electing the SBTI Safe Harbor will generally be able to treat their QTIs in non-Pillar 2 jurisdictions as Adjusted Covered Taxes prospectively and, thereby, potentially mitigate any top-up taxes under the GloBE Rules.

# Qualified Tax Incentives (QTIs)

If the tax incentive is generally available and reduces the liability for a Covered Tax of the taxpayer, then the definition will generally apply.



## Expenditure-Based Incentives

- Designed to encourage investments in a jurisdiction; typically targeted at expenditures that are expected to have positive impacts in the jurisdiction.
- Operate to reduce the taxpayer's costs by a fixed determinable amount and are calculated as a portion of costs incurred (e.g., R&D Credit)
- Must be calculated based directly on the related expenses. If the tax allowance only gives rise to timing differences, those do not fall within the definition of QTIs.
- Expenditures are incurred when accrued in the financial accounts used to calculate the income or loss or when a payment is made. May also be calculated from prior expenditures, provided they occurred after the incentive was established.



## Production-Based Incentives

- Designed to support a certain activity but not based directly on the expenditure. Can apply based on the units produced or on a reduction in negative externalities (e.g., emissions).
- Limitations of production-based incentives:
  - Only eligible when the incentive is calculated based on the volume of production.
  - Only included when they are based on the production of tangible property in the jurisdiction. This includes manufacturing activities, the production of electricity, and processing activities such as extraction and refining.
  - The incentive is based on the units produced in the jurisdiction providing the incentive.

# Calculation of QTIs

The incentive must be calculated based on expenditures incurred or output that has been produced by the time that the amount of the incentive is determined.

- An incentive is not eligible if it is calculated based on expenses or production completed before the incentive was active, or if it's determined by a promise of future spending or output when no actual costs have been incurred or units produced at the time the incentive amount is set.

**Expenditure-based** tax incentives are determined by the calculated value of the associated tax benefit. The tax benefit represents the highest possible reduction in tax liability that can be obtained through the incentive. In the case of a tax credit, the benefit is the actual amount of the credit itself.

- For incentives such as a super deduction, enhanced allowance, or exemption, the value of the tax benefit is computed by multiplying the additional deductible amount or excluded income by the applicable statutory tax rate.

**Production-based** tax incentives are generally provided in the form of a tax credit and typically calculate the amount of relief based on the amount of a defined output produced by the taxpayer.

When the SBTI Safe Harbor election is made, adjustments in respect of QTIs are made to the effective tax rate calculation for the Tested Jurisdiction. Since they are made at the jurisdictional level, they are applied after the Adjusted Covered Taxes and GloBE Income has been calculated under Chapters 3 and 4 of the GloBE Model Rules; QTIs are treated as an increase to the Adjusted Covered Taxes in the Tested Jurisdiction.

Since QTIs are not included in GloBE income, unlike Qualified Refundable Tax Credits (QRTCs) and Marketable Transferable Tax Credits (MTTCs), an MNE Group can make an annual election to treat QRTCs or MTTCs as a QTI, if they meet the definition of a QTI.

# Substance Cap in the Jurisdiction



The extent of adjustments for QTIs is limited by the Substance Cap in the jurisdiction. There are two methods to calculate the Substance Cap for the jurisdiction.

- The first method is based on the greater of 5.5% of Eligible Payroll Costs (EPC) or the depreciation on Eligible Tangible Assets (ETA).
- The second method is based on the varying values of ETAs. ETAs include the carrying value of property, plant and equipment, natural resources, and a lessee's right-of-use assets. If the MNE Group revokes this election, the assets for which carrying value was previously included in the calculation must be excluded from the calculation of the depreciation and depletion expense in method one.

# 03

Extension of the Transitional CbCR  
Safe Harbor (TCSH)



# Transitional CbCR Safe Harbor (TCSH)

The TCSH was introduced as part of the OECD's December 2022 guidance to provide temporary transitional relief as the GloBE rules came into effect.

This safe harbor allows MNE Groups to avoid detailed GloBE calculations in certain jurisdictions where they can demonstrate, based on qualifying CbCR and financial accounting data, that they meet one of the following tests:

- **De Minimis Test:** satisfied if the Tested Jurisdiction has CbCR revenue less than 10 million euro, and the CbCR profit (loss) before income tax is less than 1 million euro.
- **Routine Profits Test:** satisfied if the Tested Jurisdiction's profit or loss before income tax is equal to or less than the substance-based income, with a payroll and tangible assets carve out.
- **ETR Test:** satisfied if the computed ETR is equal to or greater than the global minimum tax transition rate.

The TCSH was made available for a transition period that covered all fiscal years beginning on or before December 31, 2026, but not after June 30, 2028. The SbS package extends the application of the TCSH to fiscal years beginning on or before December 31, 2027, but not after June 30, 2029.



# 04

## Simplified ETR Safe Harbor (SESH)



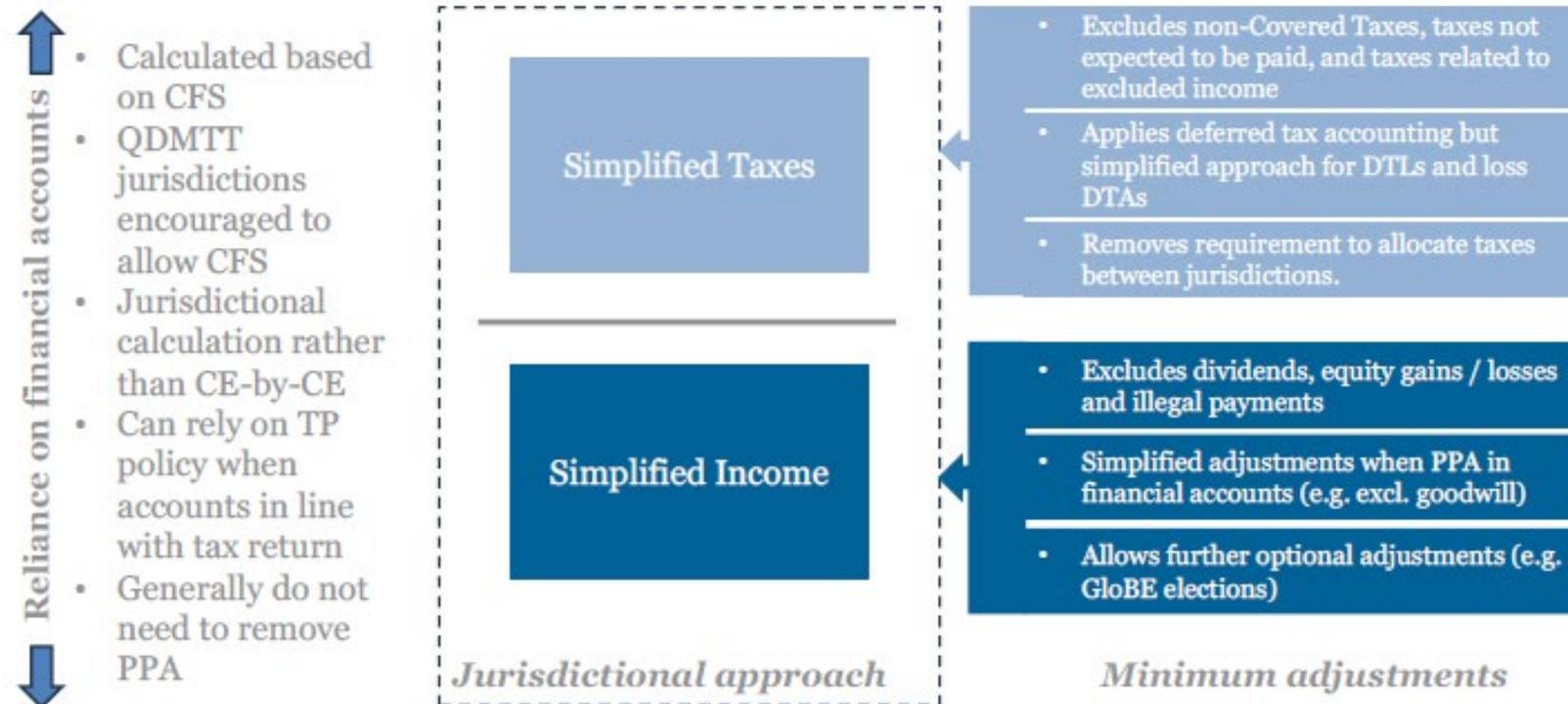
# Overview: Simplified ETR Safe Harbor



- Designed to permanently replace the ETR Test within the TCSH.
- With this safe harbor, an MNE Group's ETR is calculated simply from financial reporting data, with some adjustments.
- If the Simplified ETR for the Tested Jurisdiction is at least 15% or the Tested Jurisdiction has a simplified loss, the Top-up Tax is deemed zero and a full GloBE calculation isn't required.

# Calculating the Simplified ETR

Figure 1.1. Overview of the Simplified ETR calculation



*"Tax Challenges Arising from the Digitalisation of the Economy," Global Anti-Base Erosion Model Rules (Pillar Two), Side-by-Side Package, pg. 11, OECD 2026*

The Simplified ETR is determined by dividing the Simplified Taxes by the Simplified Income from the MNE Group's financial statements with minimal adjustments to each item.

# Elections to Consider

## M&A Simplification

- An MNE Group can apply the M&A Simplification to compute the Simplified ETR provided that all of the assets (excluding goodwill) and liabilities for which a GloBE-to-Book Difference is identified for the Tested Jurisdiction have the same tax basis before and after the M&A Transaction and corresponding deferred tax assets or liabilities accrued at a rate that equals or exceeds the Minimum Rate.
- Pursuant to the M&A Simplification:
  - The effect of the GloBE-to-Book Difference on the jurisdictional profit before tax for the Tested Jurisdiction is not removed from the computation,
  - The accrual of the deferred tax assets and liabilities arising from the M&A Transaction is not included in Simplified Taxes, and
  - The reversal of deferred tax assets and liabilities arising from the M&A Transaction, including deferred tax liabilities that are not Recapture Exception Accruals, is included in Simplified Taxes.

## Article 6.3.4 Election

- Current Year Transaction – In a year for which the SESH is elected, an MNE Group may make an election under Article 6.3.4 where the tax basis of the assets and liabilities of a Constituent Entity is adjusted to the fair value as determined in connection with a triggering event (including a triggering event related to an M&A Transaction) that occurs for local tax purposes in the current Fiscal Year.
- Prior Year Transaction – In a year for which the SESH is elected, an MNE Group may also make an election under Article 6.3.4 in relation to assets and liabilities where the tax basis of the assets and liabilities is adjusted to the fair value as determined in connection with an M&A Transaction that occurred in a prior Fiscal Year, provided that the Article 6.3.4 election was not available for that year. When an election under Article 6.3.4 is made pursuant to this paragraph, the GloBE-to-Book Difference attributable to each asset and liability is included in the computation of Simplified Income either in the year of the election or ratably over a five-year period, starting from the year of the election. The Article 6.3.4 election applies to all the assets and liabilities that were transferred in the relevant M&A Transaction.

## Chapter 3 GloBE Elections

- The GloBE elections available under Chapters 3 of the GloBE Model Rules are also available when computing the Simplified Income and Simplified Taxes. Thus, the following elections are available:
  - Inclusion of all Portfolio Shareholding dividends (Article 3.2.1(b));
  - Equity Investment Inclusion Election (Article 3.2.1(c));
  - Election to treat FX hedging as Excluded Equity Gain or Loss (Article 3.2.1(c));
  - Debt Release (Article 3.2.1(i));
  - Stock-based Compensation Election (Article 3.2.2);
  - Realization principle election (Article 3.2.5);
  - Capital gain spread over five year (Article 3.2.6), and
  - Intra-group transactions election (Article 3.2.8)

# Mechanics of the Election



- This computation is made on a jurisdictional basis and should include all entities located in the same jurisdiction in line with the GloBE Model rules.
- A Tested Jurisdiction comprises Constituent Entities, Permanent Establishments, Joint Ventures, or JV Subsidiaries for which an individual ETR calculation is mandated under the GloBE Model Rules.
  - Differs from the GloBE rules in that Investment Entities, if certain conditions are met and the MNE Group elects to do so, can be treated as residents in the same jurisdiction as other Constituent Entities for the simplified ETR Safe Harbor.
- A Filing Constituent Entity can elect the SESH for a Tested Jurisdiction for a fiscal year that commences on or after December 31, 2026.

# Pillar Two Technical Update: Key Changes to GloBE Reporting

## Open Discussion

Watch part one of this webinar: [Pillar Two Technical Series: Side-by-Side System Changes](#)



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