Medical Technology

Pillar Two and medtech tax

Industry Overview

27 November 2023

Equity
United States
Medical Technology

Travis Steed
Research Analyst
BofAS
+1 404 607 3251
travis.steed@bofa.com

Craig Bijou
Research Analyst
BofAS
+1 646 855 2590
craig.bijou@bofa.com

Stephanie Piazzola
Research Analyst
BofAS
+1 646 855 4568
stephanie.piazzola@bofa.com

Carolyn Huszagh
Research Analyst
BofAS
+1 312 259 7414
carolyn.huszagh@bofa.com

Pillar Two seems manageable; more likely 2025 not 2024

We recently spoke with a tax expert after a few medtech companies highlighted tax rates moving up next year due to Pillar Two (the 15% global minimum tax). This is not specific to medtech, but we think the impact of Pillar Two on medtech seems like a manageable headwind from the few companies that have called it out so far (tax rates moving up 100-200bps). Also, our expert thinks this headwind could materialize more in 2025 than 2024 with implementation delays. Inside we go through all the key takeaways from our tax expert call for those that want to get more into the details of Pillar Two.

Medtech so far seeing 100-200bps of higher tax rates

ZBH called out 150bps of higher tax from Pillar Two based on what has passed so far and what it expects to pass next year (ZBH has offsets elsewhere on the PnL). Alcon said Pillar Two has 200bps impact on its tax rate. JNJ called out 100bps of higher tax in 2024 from Pillar Two. COO doesn't see an impact as its already a full taxpayer. Most medtech companies already have double-digit tax rates today (see Exhibit 2) and every 100bps increase in tax rate is about 1-1.5% of EPS before any offsets (see Exhibit 3). Exhibit 1 inside has our tracker for what each company has said so far on Pillar Two.

Our expert sees 2025 as year where we see the impact

Pillar Two was supposed to go live in 2024, but our expert thinks this likely gets pushed to 2025. However, some countries passed legislation already with effective dates for 2024 given that was the expected timeline. Our tax expert believes these countries with 2024 implementation dates could also delay to 2025 to line up with other countries. However, until they do so, some companies likely presume it's the law and make tax calculations and tax forecasts consistent with the law as it is today. However, companies with significant top-up taxes may have to disclose more soon about potential liabilities as enough is known at this point about the rules to start estimating potential impacts.

Things to consider...parent domiciled in low-tax country

Our tax expert said just generally speaking companies domiciled in a low-tax country could see a higher impact given the potential for more top-up tax as most of income is typically taxed at the parent level. For example, Ireland has a 12.5% tax rate and has already announced plans to take the rate up to 15% for Pillar Two companies.

Things to consider...big benefits from R&D tax credits

Companies in the US that benefit from tax credits such as the R&D tax credit could also see an outsized impact depending on how much of a benefit they get. If the tax credit reduces overall US tax rate below 15% then Pillar Two rules could effectively reverse the benefit of these tax credits. Companies disclose in filings benefits from R&D tax credits but it's difficult to make a call on this given these are reported (not adjusted tax rates) and it's not clear if the R&D credits would be big enough to bring down overall US tax rates below 15% or not.

Abbreviations:
COO: Cooper
JNJ: Johnson and Johnson
PnL: profit and loss
ZBH: ZimmerBiomet

Refer to important disclosures on page 11 to 13.
12631732

Timestamp: 27 November 2023 06:30AM EST

See inside - we go into deep detail on things we learned from our tax expert. There are a lot of nuances with US and various forms of tax collections.

Exhibit 1: Large cap comments on 2024 tax rates and Pillar Two

The commentary from large cap companies on the Pillar Two is mixed. Some expect it to create a headwind, although several companies think they can offset the headwind at least in 2024. Others have said that it's too early to tell what the impact will be.

Company	2024 tax rate comments	Comments on Pillar Two Impact
Abbott Labs	n/a	No comments on Pillar Two
Alcon	200bps higher than fiscal 2023	"I would just keep Pillar Two in mind. So assuming Pillar Two is implemented in 2024, that has about 2 points of impact to our effective tax rate. So that's how I think about next year." *- ALC FQ3 2024 call (11/15)*
Baxter	n/a	No comments on Pillar Two
Becton Dickinson	n/a	"First of all, BD, we start our fiscal year before everyone else, so Pillar Two is not contemplated nor applicable to us in fiscal year 2024. We continue to assess those dynamics. We expect a lot more information as this year progresses. We'll share more on that at a future date. Obviously our tax rate, we are planning for a step-up in tax that we've absorbed in our guidance, but I think more to come on Pillar Two and we'll see how this plays out for us. So, we have time on that one." *- BDX FQ4 2023 call (11/9)*
Boston Scientific	In line with 2023 (14% oper. and 13% adj.)	To be clear on EU pillar II, any countries/jurisdictions that have implemented pillar II in to law today would be considered in the assumptions we shared at Investor Day. However, there continues to be uncertainty around any additional countries that will implement pillar II – any potential implementation has not been included in our assumptions. In 2026, we do expect 200-300bps of upward pressure to the rate based on TCJA provisions that are set to expire in 2026 (this is written in current legislation) *- BSX (11/11)* "we would expect our 2024 and 2025 tax rate to be in line with our original 2023 expectations of 14% operational and 13% adjusted" *- BSX Q3 call (10/26)*
The Cooper Companies	15% in fiscal 2024 (no impact from Pillar Two)	"We don't think pillar 2 will have an impact on us as we are already a full tax payor. Our organic tax rate is 15.5% and we continue to expect our tax rate to be around 15-16% going forward subject to discretes." *- COO (11/16)*
Edwards Lifesciences	n/a	No comments on Pillar Two
GE Healthcare	n/a	"we are evaluating the potential impact of Pillar 2 on our tax burden" *- GEHC (11/15)*
Intuitive Surgical	n/a	"we are aware of pillar II activities and potential changes in a number of countries, but it is too early for us to comment on whether there is a specific impact to Intuitive" *- ISRG (11/15)*
Johnson & Johnson	up to 1% higher from Pillar Two	"With respect to tax, as you may be aware, the European Union member states are in the process of enacting the EU's Pillar 2 directive which generally provides for a 15% minimum tax rate as established by the OECD Pillar 2 framework. The first EU effective date for certain aspects of the law is January 1, 2024. As a result, we currently estimated up to 1% tax rate increase in 2024. In addition, the US Treasury's current perspective on Pillar 2 will be harmful as it relates to the treatment of US incentives for innovation and will result in US based multinational companies paying more tax revenue to foreign governments." *- JNJ Q3 call (10/17)*
Medtronic	n/a	"Global tax reform will likely be a headwind but as always, we're focused on driving offsets everywhere that we can. *- MDT FQ2 call (11/21)*
Stryker	Won't be materially higher than 2023 (14%) (no expected impact from Pillar Two)	"Pillar 2 tax so what we've said on the earnings call is we believe we're going to be okay for 2024. We are aware that doesn't impact, but we have tax planning strategies that can get us through 2024. Not sure yet on 2025 and beyond... ...We'll provide guidance in January, but we're not – I know other companies have kind of flagged 2024 being a challenge. I think you could expect a more normal year in 2024. So this year we're guiding to 14%. That's a little bit low because we had some discrete items, but it won't be materially higher than that next year. We're still working on plans for 2025 and beyond. So there could be an impact and potentially in 2025." *- SYK Analyst Day (11/10)* "Just to finish on tax, as it relates to PILLAR II, at this point we're not projecting really anything negative next year if you think about our overall tax position, but of course we'll include that in our guidance early next year." *- SYK Q3 call (11/2)*
Teleflex Inc	overall tax rate modestly higher than 2023 (11%) (includes any Pillar Two impact)	"Tom's comment about an increase in the tax rate for 2024 did include assumptions for Pillar 2. We have not finished up our annual plan for 2024, so not in a position to provide guidance at this time. For context, recall that the assumption in the LRP was for a 12% tax rate, so that should help provide some sense of direction." *- TFX (11/15)* "So we're not in a position to provide specific guidance for 2024 at this point. I would say that the expectation would be that the tax rate would be modestly higher than where we are in 2023." *- TFX Q3 call (11/2)*
Zimmer Biomet	+150bps over 2023 (includes any Pillar Two impact)	"Our updated tax expectations due to Pillar II are based on what has passed and what we expect to occur next year. We saw the headwind and didn't want to surprise the Street with a sizeable tax step up so we wanted to call it out as early as possible. With that said, we believe we'll offset much of that headwind and continue to grow EPS faster than revenue. We'll certainly update the street should there be a material change in our expected 2024 tax rate as we go forward." *- ZBH (11/22)* "...we do see a higher tax rate for next year because of the OECD's Pillar Two...On the tax rate, right now our best estimate is that it'll be about a 150 basis point increase off of our full year 2023 tax rate." *- ZBH Q3 call (11/7)*

Exhibit 1: Large cap comments on 2024 tax rates and Pillar Two

The commentary from large cap companies on the Pillar Two is mixed. Some expect it to create a headwind, although several companies think they can offset the headwind at least in 2024. Others have said that it's too early to tell what the impact will be.

Source: Company filings, BofA Global Research

BofA GLOBAL RESEARCH

Exhibit 2: Large cap medtech tax rates and what we model for 2024/2025

We model higher tax rates in 2024/2025 for almost all of our covered large cap companies

Company	2018	2019	2020	2021	2022	2023	2024	2025
Abbott Labs	14.1%	14.0%	15.0%	15.5%	15.7%	14.0%	14.5%	14.5%
Baxter	17.7%	16.7%	16.7%	16.8%	19.9%	20.8%	21.0%	21.0%
Becton Dickinson	16.7%	14.4%	14.5%	11.4%	13.3%	12.9%	13.8%	14.0%
Boston Scientific	6.8%	7.3%	5.3%	7.6%	12.7%	12.0%	13.2%	13.2%
The Cooper Companies	7.7%	6.6%	10.7%	11.2%	12.9%	13.2%	15.0%	15.0%
Edwards Lifesciences	13.4%	11.5%	12.5%	12.6%	14.6%	16.4%	15.0%	14.0%
GE Healthcare	n/a	17.1%	22.8%	23.6%	22.5%	24.3%	24.0%	24.0%
Intuitive Surgical	19.6%	19.5%	22.5%	22.2%	21.8%	22.5%	22.5%	22.5%
Medtronic	14.7%	13.6%	14.3%	11.8%	12.7%	13.7%	15.9%	17.5%
Stryker	16.7%	15.8%	12.6%	14.9%	14.0%	13.8%	15.0%	15.0%
Teleflex Inc	11.9%	11.2%	11.1%	13.3%	11.9%	10.3%	12.0%	12.0%
Zimmer Biomet	18.0%	16.8%	16.0%	15.7%	16.5%	16.5%	18.0%	18.0%

Source: Company filings; BofA Global Research

MDT, BDX and COO are fiscal years; Green represents our tax rate estimates

BofA GLOBAL RESEARCH

Exhibit 3: Potential EPS impact of 1% higher tax rate in 2024 and 2025

This table shows the potential EPS impact for large cap medtech companies if their respective tax rates were to increase by 100bps in 2024 and/or 2025.

	Street/Cons EPS		Tax Rate Change		EPS $ Impact		EPS % Impact	
Company	2024E	2025E	2024E	2025E	2024E	2025E	2024E	2025E
Abbott Labs	$ 4.62	$ 5.13	1.0%	1.0%	$(0.05)	$(0.06)	(1.2%)	(1.2%)
Baxter	$ 3.04	$ 3.42	1.0%	1.0%	$(0.04)	$(0.04)	(1.3%)	(1.3%)
Becton Dickinson	$ 12.83	$ 14.32	1.0%	1.0%	$(0.15)	$(0.17)	(1.2%)	(1.2%)
Boston Scientific	$ 2.24	$ 2.52	1.0%	1.0%	$(0.03)	$(0.03)	(1.1%)	(1.2%)
The Cooper Companies	$ 14.10	$ 16.26	1.0%	1.0%	$(0.17)	$(0.19)	(1.2%)	(1.2%)
Edwards Lifesciences	$ 2.82	$ 3.18	1.0%	1.0%	$(0.03)	$(0.04)	(1.2%)	(1.2%)
GE Healthcare	$ 4.27	$ 4.84	1.0%	1.0%	$(0.06)	$(0.06)	(1.3%)	(1.3%)
Intuitive Surgical	$ 6.31	$ 7.28	1.0%	1.0%	$(0.08)	$(0.09)	(1.3%)	(1.3%)
Medtronic	$ 5.16	$ 5.44	1.0%	1.0%	$(0.06)	$(0.07)	(1.2%)	(1.2%)
Stryker	$ 11.54	$ 12.80	1.0%	1.0%	$(0.14)	$(0.15)	(1.2%)	(1.2%)
Teleflex Inc	$ 13.93	$ 15.76	1.0%	1.0%	$(0.16)	$(0.18)	(1.1%)	(1.1%)
Zimmer Biomet	$ 7.95	$ 8.50	1.0%	1.0%	$(0.10)	$(0.10)	(1.2%)	(1.2%)

Source: Company filings, Bloomberg, BofA Global Research

MDT, BDX and COO EPS are fiscal years

BofA GLOBAL RESEARCH

Exhibit 4: Status of countries planning to implement Pillar Two

Only 4 countries have adopted final legislation implementing one of the Pillar Two rules; however 25 countries have draft legislation for Pillar Two

Final Legislation		Draft Legislation		Intend to Implement
Jurisdiction	**Pillar Two Rules**	**Jurisdiction**	**Pillar Two Rules**	**Jurisdiction**
European Union	QDMTT, IIR, UTPR	Austria	QDMTT, IIR, UTPR	Australia
Japan	QDMTT, IIR, UTPR	Bulgaria	QDMTT, IIR, UTPR	Bahamas
Mauritius	QDMTT	Canada	QDMTT, IIR	Belgium
South Korea	IIR, UTPR	Cyprus	QDMTT, IIR, UTPR	Gibraltar
United Kingdom	QDMTT, IIR	Czech Republic	QDMTT, IIR, UTPR	Guernsey
		Denmark	QDMTT, IIR, UTPR	Hong Kong
		Finland	QDMTT, IIR, UTPR	Indonesia
		France	QDMTT, IIR, UTPR	Isle of Man
		Germany	QDMTT, IIR, UTPR	Jersey
		Hungary	QDMTT, IIR, UTPR	Malaysia
		Ireland	QDMTT, IIR, UTPR	Malta
		Italy	QDMTT, IIR, UTPR	Qatar
		Liechtenstein	QDMTT, IIR, UTPR	Singapore
		Lithuania	Filing obligations	South Africa
		Luxembourg	QDMTT, IIR, UTPR	Spain
		Netherlands	QDMTT, IIR, UTPR	Taiwan
		New Zealand	IIR, UTPR	Thailand
		Norway	QDMTT, IIR	United Arab Emirates
		Romania	QDMTT, IIR, UTPR	
		Slovakia	QDMTT	
		Slovenia	QDMTT, IIR, UTPR	
		Sweden	QDMTT, IIR, UTPR	
		Switzerland	QDMTT, IIR, UTPR	
		United Kingdom	UTPR	
		Vietnam	QDMTT, IIR	

Source: Ernst & Young, BofA Global Research. QDMTT: Qualified Domestic Minimum Top-up Tax; UTPR: Undertaxed Profits Rule; IIR: Income Inclusion Rule.

BofA GLOBAL RESEARCH

Pillar II takeaways from our Tax Expert

We conducted a call with a tax expert to discuss the details behind Pillar Two and the potential impact on the tax rates. See below for all our takeaways, but these were a few key things that stood out:

- The intention of the Pillar Two rules is to create a global minimum corporate tax rate of 15%.
- The OECD provided rules for the countries to follow but each country has to pass its own tax legislation.
- Pillar Two likely will not go into effect until 2025 and any countries that intended to implement new tax legislation for Pillar Two in 2024 will likely defer until 2025. But countries that have already passed legislation still have their laws saying 2024 and have not updated for 2025 yet.
- We are unlikely to see any companies with corporate tax rates well below 15% post Pillar Two. Some could be above 15% though.
- US is not compliant with Pillar Two and it is not expected to be, but that doesn't mean there won't be an impact. There are various forms of collecting tax as we explain below. Worst case some US companies may have to pay the tax to other countries (pending how things work out) especially if they benefit from tax credits like the R&D tax credit that pushes their US tax rate below 15%.
- Companies parented in low tax jurisdictions more likely to pay top-up tax.

- All countries in the OECD appear onboard with the Pillar Two rules today but there is likely to be more negotiations and discussions as implementation gets closer.

Pillar 2 thoughts from our tax expert

Global minimum tax regardless of tax structure of incentives

Countries have been dealing with international tax arbitrage for decades and as systems continue to become more complicated this arbitrage is getting more difficult. The OECD took it upon itself to create a global minimum tax regime to create a floor regardless of what local tax rules are and all the different eccentricities each country has in their tax system. If you are operating in a country, the idea is that you need to be paying a certain amount of tax regardless of incentives negotiated. That is the principle behind the system.

At its basic concept you compare the tax paid compared to pre-tax income and if its 15% or higher, then it meets the standards. This is done on a country-by-country basis. If its below 15% in a particular country it requires a company to pay that tax to the other countries (called a top-up tax) to make up for the tax not paid in the lower tax country.

This has created a situation for lower tax countries. If other countries are going to collect the top-up tax from income earned in your lower tax country then the lower tax country would rather collect that tax. Therefore QDMTT (Qualified Domestic Minimum Top-up Tax) that is a rule OECD has developed as part of the system and that rule is basically a local country can just put in a minimum tax locally that requires them to pay 15% locally regardless of what all other rules say. Then the lower tax country can collect the top-up tax rather than other countries collecting it. There are a lot of countries that are already planning to implement the QDMTT not surprisingly as they would rather receive the tax if it has to be paid either way.

OECD provides language for countries to implement into law

Anything going on in any country also needs to go through whatever the local laws are to enact these changes. OECD is not a governmental entity. OECD is basically providing all the countries that will be participating with statutory language. They frame it as articles that looks like statutory language. Some countries have specific concepts where they must adapt what the OECD has to their specific code of laws. Every country in theory will implement these rules by enacting new legislation, except the US for now.

US having a hard time agreeing – OECD developing specific US rules

The US Congress is having a hard time agreeing, and there also does not seem to be much appetite to implement. It seems unlikely the US will implement any statutory changes anytime soon. The OECD has tried to come up with special rules to deal with the US since the US is such a big piece of the global economy. They are developing rules to deal with the fact that the US rules are not strictly compliant with the OECD rules.

The collection mechanism in the US would be UTPR rule (undertaxed profits rule) in local countries (we explain more at end of this note). Even if the US doesn't change anything, if all the other countries implement the UTPR rule, those countries will collect that tax even though the US hasn't changed its rules. The system has been developed even though the US hasn't adopted it. The way the system will work is that as long as other countries go along with it, a company will end up having to pay this tax even if your local country doesn't go along with it. That is likely by design to convince every country to adopt. This is why countries are basically doing QDMTT now because if the tax is going to be collected, they might as be the ones to collect it.

Low tax jurisdictions unlikely to give other offsets – tax not lower elsewhere

Some companies have very low effective tax rates today as they tend to operate in a couple of low tax jurisdictions – Switzerland and Singapore, to a lesser extent Ireland – where they have worked out or negotiated very good tax incentives and have very low or zero tax rates in those countries. There is a question if these countries will provide other non-tax incentives to try to offset the cost of the extra tax if they adopt a QDMTT. However, there doesn't seem to be a huge appetite to provide other offsets given the companies are already located in these countries and can't move and obtain a lower tax rate because other places are subject to the same rules as well.

2024 is first live year officially but likely getting pushed more to 2025

Some countries – Korea and a couple of other countries – have already implemented QDMTTs that would take effect in 2024 as this was going to be the first live year for Pillar 2. But our expert sees this being pushed to 2025 now. However, some countries that were early adopters and put legislation in place were putting 2024 effective dates in the legislation. Our expert believes these countries likely amend and change their legislation to 2025 as well. However, until they do so, companies likely have to presume it's the law and have to make their tax calculations and tax forecasts consistent with the law as it is today.

Deferred taxes an example of why this still gets delayed to 2025

Per our expert, by and large every country has at least said that they are supportive. As its coming toward the actual date of implementation the negotiations are becoming more down to the wire. For example, the treatment of deferred taxes is a really big issue for the whole system to set up and run correctly. There are countries that are starting to signal that they are not really happy with what's been done with deferred taxes. The UK came out with proposed legislation where they diverted from the OECD current rules about how deferred taxes would work. Other counties may now need to think about deferred taxes more deeply. It's possible that there are going to be more tweaks and changes, but more guidance is coming out next month; however some of these bigger issues will not be in this guidance. Our expert says it will be interesting to see how long any of these big issues stay uncertain during 2024. At some point, there must be clarity because the laws need to go through the legislative functions in local countries.

Companies parented in low tax jurisdictions are more likely to pay top-up tax

Generally, the parent jurisdiction is where you have the potential most concern for top-up tax just because in most systems most of the income is getting taxed at the parent level. For example, for an Irish-parented entity. Ireland currently has a 12.5% rate which is below the 15% rate. Ireland has already announced plans to increase that 12.5% rate up to 15% for companies that are subject to Pillar 2. Our expert thinks it is much more likely that companies that are parented in low tax jurisdictions such are Ireland or other places are going to be more likely to pay top-up tax.

Could be above/below 15% but not drastically below 15%

There are potential scenarios where you could be a little bit below 15%. But our expert does not anticipate seeing companies dramatically below 15%. There are some aspects of the way things work today that might create a situation where planning opportunities may allow you sidestep Pillar 2 rules. But people are identifying relatively quickly and the OECD is becoming aware of them and they are implementing additional rules to shut them down.

Companies may need to make disclosure in Q4 of this year

Some companies may need to start making some disclosures in Q4 of this year given there is enough certainty in these rules that companies know what's coming. Even though it's not law yet companies that have a significant top-up tax may feel the need to make some disclosures about that in Q4. There is not a lot of specificity on what disclosures need to be made though.

Enforcement is every country's existing tax enforcement rules

The enforcement mechanism is that every country will have to implement these rules in their local tax system. It will rely on preexisting tax enforcement rules in each country to enforce the changes that Pillar 2 is making. OECD is trying to graft this on to the existing global system in a way that allows it to be consistent. Negotiated amongst all the countries first. It will rely on existing enforcement mechanism.

One concern is maintaining consensus long-term

This system is designed to be put in place on Jan 1 2025, that everybody has the same rules. But what happens after that? There is real concern from OECD and it has been a struggle to bring everyone to the table and achieve a consensus for this moment in time per our expert. How are you going to maintain consensus going forward a year from now or 5 years from now? What happens when a local country has a local program it needs to fund and increases the 15% to 17.5% to make more money? There is a real question about how this system will hold together as we move forward longer term.

Pillar 2 top-up tax mechanics – an example of no outs…

Pillar 2 has a couple of different mechanisms to claim the top-up tax. The top-up tax is the extra tax that the system says needs to be paid. There are a couple of different ways that the system will impose that tax as we show in the example below.

Take for example a US company that owns an Irish entity and is not paying 15%. There is a top-up tax owed with respect to the Irish operations. Does Ireland have a QDMTT? If Ireland has a QDMTT, then they are going to pay the extra tax to Ireland. Ireland will be at 15%. Then nobody else needs to collect any tax because the extra tax has been collected in Ireland through the QDMTT.

If Ireland doesn't implement a QDMTT, then the next defense is the Income Inclusion Rule (IIR). That is a term for a concept like the US. US has concept called Subpart F that if a foreign subsidiary earns a certain type of income, then that income even before its distributed is taxed in the US, so its taxed immediately. The premise being usually this is mobile types of income (i.e., IRS saying you should have earned that income in the US). In this example the income would be included in a US tax return. However, the OECD requires the IIR to operate a very specific way and the US rules do not operate in the way OECD has laid out. The US income inclusion rules are not compliant with the OECD.

However, if the US did have a compliant IIR, then the US would effectively collect the extra tax in the US. The additional 2.5% from Ireland's 12.5% and the 15% minimum would be collected through the IIR in the US.

The third backstop is the UTPR – Under Tax Payments Rule. UTPR says if you are in Ireland, you are US parented, in Ireland you're not paying enough tax, the US did not collect the tax because they didn't change the rules. So the system will say that every other country you operate in – so say in addition to Ireland you are in the UK and Singapore. UK and Singapore you get to collect the tax that they didn't pay in Ireland. There is a calculation that you do based on how big your presence is in each country where they split the top-up tax liability in each of those countries. You pay the top-up tax partially in Singapore and partially in the UK instead. You can have countries collecting taxes for other countries under this system. Most countries will end up with the QDMTT, but in theory these are the three mechanisms of ways you can collect tax.

R&D tax credit could make US more of a burden

Our expert said the US could end up being the biggest problem for a lot of companies that benefit from tax credits. Tax credits function to reduce tax liability, but problem is absence a specific rule, if you get tax credits that bring your tax rate below 15% then pillar 2 rules would come along and effectively reverse the benefit of those tax credits.

The R&D credit is still a so-called bad credit, meaning that you don't get to count it in your tax rate. There is a concept of a refundable credit or a good credit meaning even if you use the credit to reduce your liability you get to ignore that reduction when testing effective tax rate. The R&D credit in US is not a good credit. It is a bad credit meaning that you don't get to make that adjustment. If a company theoretically wiped out all of their tax liability with an R&D credit under pillar 2 rules the US would look like a zero rate jurisdiction and the rules say that you need to be paying 15%.

Then in the US, you have to go through the series of 3 payment options. The first one is QDMTT. US has not implemented the QDMTT. The corporate minimum tax that was implemented last year does not qualify as a QDMTT. It does not qualify as a pillar 2 compliant minimum tax. That basically preserves the benefit of R&D credit and GBC. Even with the corporate minimum tax still paying very little tax in the US. IIR rule is not an option because no one above the US to pick up the tax. The last option is the UTPR. You could end up paying the extra tax to all of the countries you operate in that you arguably should have paid in the US.

Pillar II background – what is it in our own words

Pillar Two is a set of rules designed to require multinational companies to pay the global minimum tax of 15% on profits in each country in which it operates. Pillar Two is a part of an international tax framework, designed by the Organisation for Economic Co-operation and Development (OECD) and G20 countries to address global tax avoidance and improve international tax coherence and transparency. Specifically, the OECD is attempting to stop the "race-to-the-bottom" competition where countries try to entice multinational companies with more favorable tax rates. Any multinational companies with more than 750 million Euro in revenue are subject to Pillar Two.

Pillar Two rules suggest a "top-up" tax on profits in any jurisdiction where the effective tax rate falls below the 15% global minimum tax. For example, Ireland had a 12.5% tax on corporate profits. Under Pillar Two, companies would need to pay an extra 2.5% of tax on profits made in Ireland. There are three principal tax calculation methods that a jurisdiction can use to be in compliance – the Qualified Domestic Minimum Top-Up Taxes (QDMTT), Income Inclusion Rule (IIR) and the Undertaxed Payments Rule (UTPR). Most jurisdictions are likely to implement QDMTT which requires any jurisdiction under the minimum global tax to raise its tax rate to the global minimum or add an incremental tax on top of its current tax. The IIR allows a multinational's home country to tax the company's foreign profits. The UTPR is a backstop that allows each country where a multinational has operations to collect a portion of the company's top-up tax if the home country has not implemented a QDMTT or IIR rule.

Pillar Two represents OECD's recommended template for each individual country or jurisdiction to use to enact new local tax legislation. The majority of the 135+ countries represented by the OECD/G20 are in the process of adopting new legislation or have stated that they intend to do so. According to our tax expert, only four countries (and the European Union) have finalized new tax legislation. Pillar Two was supposed to go into effect at the start of 2024 but the tax expert we spoke to expects the implementation to be pushed to 2025.

Disclosures

Important Disclosures

FUNDAMENTAL EQUITY OPINION KEY: Opinions include a Volatility Risk Rating, an Investment Rating and an Income Rating. VOLATILITY RISK RATINGS, indicators of potential price fluctuation, are: A - Low, B - Medium and C - High. INVESTMENT RATINGS reflect the analyst's assessment of both a stock's absolute total return potential as well as its attractiveness for investment relative to other stocks within its Coverage Cluster (defined below). Our investment ratings are: 1 - Buy stocks are expected to have a total return of at least 10% and are the most attractive stocks in the coverage cluster; 2 - Neutral stocks are expected to remain flat or increase in value and are less attractive than Buy rated stocks and 3 - Underperform stocks are the least attractive stocks in a coverage cluster. An investment rating of 6 (No Rating) indicates that a stock is no longer trading on the basis of fundamentals. Analysts assign investment ratings considering, among other things, the 0-12 month total return expectation for a stock and the firm's guidelines for ratings dispersions (shown in the table below). The current price objective for a stock should be referenced to better understand the total return expectation at any given time. The price objective reflects the analyst's view of the potential price appreciation (depreciation).

Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster[R1]
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

[R1] Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

INCOME RATINGS, indicators of potential cash dividends, are: 7 - same/higher (dividend considered to be secure), 8 - same/lower (dividend not considered to be secure) and 9 - pays no cash dividend. *Coverage Cluster* is comprised of stocks covered by a single analyst or two or more analysts sharing a common industry, sector, region or other classification(s). A stock's coverage cluster is included in the most recent BofA Global Research report referencing the stock.

BofA Global Research personnel (including the analyst(s) responsible for this report) receive compensation based upon, among other factors, the overall profitability of Bank of America Corporation, including profits derived from investment banking. The analyst(s) responsible for this report may also receive compensation based upon, among other factors, the overall profitability of the Bank's sales and trading businesses relating to the class of securities or financial instruments for which such analyst is responsible.

Other Important Disclosures

From time to time research analysts conduct site visits of covered issuers. BofA Global Research policies prohibit research analysts from accepting payment or reimbursement for travel expenses from the issuer for such visits.

Prices are indicative and for information purposes only. Except as otherwise stated in the report, for any recommendation in relation to an equity security, the price referenced is the publicly traded price of the security as of close of business on the day prior to the date of the report or, if the report is published during intraday trading, the price referenced is indicative of the traded price as of the date and time of the report and in relation to a debt security (including equity preferred and CDS), prices are indicative as of the date and time of the report and are from various sources including BofA Securities trading desks.

The date and time of completion of the production of any recommendation in this report shall be the date and time of dissemination of this report as recorded in the report timestamp.

Recipients who are not institutional investors or market professionals should seek the advice of their independent financial advisor before considering information in this report in connection with any investment decision, or for a necessary explanation of its contents.

Officers of BofAS or one or more of its affiliates (other than research analysts) may have a financial interest in securities of the issuer(s) or in related investments.

Refer to BofA Global Research policies relating to conflicts of interest.

"BofA Securities" includes BofA Securities, Inc. ("BofAS") and its affiliates. Investors should contact their BofA Securities representative or Merrill Global Wealth Management financial advisor if they have questions concerning this report or concerning the appropriateness of any investment idea described herein for such investor. "BofA Securities" is a global brand for BofA Global Research.

Information relating to Non-US affiliates of BofA Securities and Distribution of Affiliate Research Reports:

BofAS and/or Merrill Lynch, Pierce, Fenner & Smith Incorporated ("MLPF&S") may in the future distribute, information of the following non-US affiliates in the US (short name: legal name, regulator): Merrill Lynch (South Africa): Merrill Lynch South Africa (Pty) Ltd., regulated by The Financial Service Board; MLI (UK): Merrill Lynch International, regulated by the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA); BofASE (France): BofA Securities Europe SA is authorized by the Autorité de Contrôle Prudentiel et de Résolution (ACPR) and regulated by the ACPR and the Autorité des Marchés Financiers (AMF). BofA Securities Europe SA ("BofASE") with registered address at 51, rue La Boétie, 75008 Paris is registered under no 842 602 690 RCS Paris. In accordance with the provisions of French Code Monétaire et Financier (Monetary and Financial Code), BofASE is an établissement de crédit et d'investissement (credit and investment institution) that is authorised and supervised by the European Central Bank and the Autorité de Contrôle Prudentiel et de Résolution (ACPR) and regulated by the ACPR and the Autorité des Marchés Financiers. BofASE's share capital can be found at www.bofaml.com/BofASEdisclaimer; BofA Europe (Milan): Bank of America Europe Designated Activity Company, Milan Branch, regulated by the Bank of Italy, the European Central Bank (ECB) and the Central Bank of Ireland (CBI); BofA Europe (Frankfurt): Bank of America Europe Designated Activity Company, Frankfurt Branch regulated by BaFin, the ECB and the CBI; BofA Europe (Madrid): Bank of America Europe Designated Activity Company, Sucursal en España, regulated by the Bank of Spain, the ECB and the CBI; Merrill Lynch (Australia): Merrill Lynch Equities (Australia) Limited, regulated by the Australian Securities and Investments Commission; Merrill Lynch (Hong Kong): Merrill Lynch (Asia Pacific) Limited, regulated by the Hong Kong Securities and Futures Commission (HKSFC); Merrill Lynch (Singapore): Merrill Lynch (Singapore) Pte Ltd, regulated by the Monetary Authority of Singapore (MAS); Merrill Lynch (Canada): Merrill Lynch Canada Inc, regulated by the Canadian Investment Regulatory Organization; Merrill Lynch (Mexico): Merrill Lynch Mexico, SA de CV, Casa de Bolsa, regulated by the Comisión Nacional Bancaria y de Valores; Merrill Lynch (Argentina): Merrill Lynch Argentina SA, regulated by Comisión Nacional de Valores; BofAS Japan: BofA Securities Japan Co., Ltd., regulated by the Financial Services Agency; Merrill Lynch (Seoul): Merrill Lynch International, LLC Seoul Branch, regulated by the Financial Supervisory Service; Merrill Lynch (Taiwan): Merrill Lynch Securities (Taiwan) Ltd., regulated by the Securities and Futures Bureau; BofAS India: BofA Securities India Limited, regulated by the Securities and Exchange Board of India (SEBI); Merrill Lynch (Israel): Merrill Lynch Israel Limited, regulated by Israel Securities Authority; Merrill Lynch (DIFC): Merrill Lynch International (DIFC Branch), regulated by the Dubai Financial Services Authority (DFSA); Merrill Lynch (Brazil): Merrill Lynch S.A. Corretora de Títulos e Valores Mobiliários, regulated by Comissão de Valores Mobiliários; Merrill Lynch KSA Company: Merrill Lynch Kingdom of Saudi Arabia Company, regulated by the Capital Market Authority.

This information: has been approved for publication and is distributed in the United Kingdom (UK) to professional clients and eligible counterparties (as each is defined in the rules of the FCA and the PRA) by MLI (UK), which is authorized by the PRA and regulated by the FCA and the PRA - details about the extent of our regulation by the FCA and PRA are available from us on request; has been approved for publication and is distributed in the European Economic Area (EEA) by BofASE (France), which is authorized by the ACPR and regulated by the ACPR and the AMF; has been considered and distributed in Japan by BofAS Japan, a registered securities dealer under the Financial Instruments and Exchange Act in Japan, or its permitted affiliates; is issued and distributed in Hong Kong by Merrill Lynch (Hong Kong) which is regulated by HKSFC; is issued and distributed in Taiwan by Merrill Lynch (Taiwan); is issued and distributed in India by BofAS India; and is issued and distributed in Singapore to institutional investors and/or accredited investors (each as defined under the Financial Advisers Regulations) by Merrill Lynch (Singapore) (Company Registration No 198602883D). Merrill Lynch (Singapore) is regulated by MAS. Merrill Lynch Equities (Australia) Limited (ABN 65 006 276 795), AFS License 235132 (MLEA) distributes this information in Australia only to 'Wholesale' clients as defined by s.761G of the Corporations Act 2001. With the exception of Bank of America N.A., Australia Branch, neither MLEA nor any of its affiliates involved in preparing this information is an Authorised Deposit-Taking Institution under the Banking Act 1959 nor regulated by the Australian Prudential Regulation Authority. No approval is required for publication or distribution of this information in Brazil and its local distribution is by Merrill Lynch (Brazil) in accordance with applicable regulations. Merrill Lynch (DIFC) is authorized and regulated by the DFSA. Information prepared and issued by Merrill Lynch (DIFC) is done so in accordance with the requirements of the DFSA conduct of business rules. BofA Europe (Frankfurt) distributes this information in Germany and is regulated by BaFin, the ECB and the CBI. BofA Securities entities, including BofA Europe and BofASE (France), may outsource/delegate the marketing and/or provision of certain research services or aspects of research services to other branches or members of the BofA Securities group. You may be contacted by a different BofA Securities entity acting for and on behalf of your service provider where permitted by applicable law. This does not change your service provider. Please refer to the Electronic Communications Disclaimers for further information.

This information has been prepared and issued by BofAS and/or one or more of its non-US affiliates. The author(s) of this information may not be licensed to carry on regulated activities in your jurisdiction and, if not licensed, do not hold themselves out as being able to do so. BofAS and/or MLPF&S is the distributor of this information in the US and accepts full responsibility for information distributed to BofAS and/or MLPF&S clients in the US by its non-US affiliates. Any US person receiving this information and wishing to effect any transaction in any security discussed herein should do so through BofAS and/or MLPF&S and not such foreign affiliates. Hong Kong recipients of this information should contact Merrill Lynch (Asia Pacific) Limited in respect of any matters relating to dealing in securities or provision of specific advice on securities or any other matters arising from, or in connection with, this information. Singapore recipients of this information should contact Merrill Lynch (Singapore) Pte Ltd in respect of any matters arising from, or in connection with, this information. For clients that are not accredited investors, expert investors or institutional investors Merrill Lynch (Singapore) Pte Ltd accepts full responsibility for the contents of this information distributed to such clients in Singapore.

General Investment Related Disclosures:

Taiwan Readers: Neither the information nor any opinion expressed herein constitutes an offer or a solicitation of an offer to transact in any securities or other financial instrument. No part of this report may be used or reproduced or quoted in any manner whatsoever in Taiwan by the press or any other person without the express written consent of BofA Securities.

This document provides general information only, and has been prepared for, and is intended for general distribution to, BofA Securities clients. Neither the information nor any opinion expressed constitutes an offer or an invitation to make an offer, to buy or sell any securities or other financial instrument or any derivative related to such securities or instruments (e.g., options, futures, warrants, and contracts for differences). This document is not intended to provide personal investment advice and it does not take into account the specific investment objectives, financial situation and the particular needs of, and is not directed to, any specific person(s). This document and its content do not constitute, and should not be considered to constitute, investment advice for purposes of ERISA, the US tax code, the Investment Advisers Act or otherwise. Investors should seek financial advice regarding the appropriateness of investing in financial instruments and implementing investment strategies discussed or recommended in this document and should understand that statements regarding future prospects may not be realized. Any decision to purchase or subscribe for securities in any offering must be based solely on existing public information on such security or the information in the prospectus or other offering document issued in connection with such offering, and not on this document.

Securities and other financial instruments referred to herein, or recommended, offered or sold by BofA Securities, are not insured by the Federal Deposit Insurance Corporation and are not deposits or other obligations of any insured depository institution (including, Bank of America, N.A.). Investments in general and, derivatives, in particular, involve numerous risks, including, among others, market risk, counterparty default risk and liquidity risk. No security, financial instrument or derivative is suitable for all investors. Digital assets are extremely speculative, volatile and are largely unregulated. In some cases, securities and other financial instruments may be difficult to value or sell and reliable information about the value or risks related to the security or financial instrument may be difficult to obtain. Investors should note that income from such securities and other financial instruments, if any, may fluctuate and that price or value of such securities and instruments may rise or fall and, in some cases, investors may lose their entire principal investment. Past performance is not necessarily a guide to future performance. Levels and basis for taxation may change.

This report may contain a short-term trading idea or recommendation, which highlights a specific near-term catalyst or event impacting the issuer or the market that is anticipated to have a short-term price impact on the equity securities of the issuer. Short-term trading ideas and recommendations are different from and do not affect a stock's fundamental equity rating, which reflects both a longer term total return expectation and attractiveness for investment relative to other stocks within its Coverage Cluster. Short-term trading ideas and recommendations may be more or less positive than a stock's fundamental equity rating.

BofA Securities is aware that the implementation of the ideas expressed in this report may depend upon an investor's ability to "short" securities or other financial instruments and that such action may be limited by regulations prohibiting or restricting "shortselling" in many jurisdictions. Investors are urged to seek advice regarding the applicability of such regulations prior to executing any short idea contained in this report.

Foreign currency rates of exchange may adversely affect the value, price or income of any security or financial instrument mentioned herein. Investors in such securities and instruments, including ADRs, effectively assume currency risk.

BofAS or one of its affiliates is a regular issuer of traded financial instruments linked to securities that may have been recommended in this report. BofAS or one of its affiliates may, at any time, hold a trading position (long or short) in the securities and financial instruments discussed in this report.

BofA Securities, through business units other than BofA Global Research, may have issued and may in the future issue trading ideas or recommendations that are inconsistent with, and reach different conclusions from, the information presented herein. Such ideas or recommendations may reflect different time frames, assumptions, views and analytical methods of the persons who prepared them, and BofA Securities is under no obligation to ensure that such other trading ideas or recommendations are brought to the attention of any recipient of this information.

In the event that the recipient received this information pursuant to a contract between the recipient and BofAS for the provision of research services for a separate fee, and in connection therewith BofAS may be deemed to be acting as an investment adviser, such status relates, if at all, solely to the person with whom BofAS has contracted directly and does not extend beyond the delivery of this report (unless otherwise agreed specifically in writing by BofAS). If such recipient uses the services of BofAS in connection with the sale or purchase of a security referred to herein, BofAS may act as principal for its own account or as agent for another person. BofAS is and continues to act solely as a broker-dealer in connection with the execution of any transactions, including transactions in any securities referred to herein.

Copyright and General Information:

Materials prepared by BofA Global Research personnel are based on public information. Facts and views presented in this material have not been reviewed by, and may not reflect information known to, professionals in other business areas of BofA Securities, including investment banking personnel. BofA Securities has established information barriers between BofA Global Research and certain business groups. As a result, BofA Securities does not disclose certain client relationships with, or compensation received from, such issuers. To the extent this material discusses any legal proceeding or issues, it has not been prepared as nor is it intended to express any legal conclusion, opinion or advice. Investors should consult their own legal advisers as to issues of law relating to the subject matter of this material. BofA Global Research personnel's knowledge of legal proceedings in which any BofA Securities entity and/or its directors, officers and employees may be plaintiffs, defendants, co-defendants or co-plaintiffs with or involving issuers mentioned in this material is based on public information. Facts and views presented in this material that relate to any such proceedings have not been reviewed by, discussed with, and may not reflect information known to, professionals in other business areas of BofA Securities in connection with the legal proceedings or matters relevant to such proceedings.

This information has been prepared independently of any issuer of securities mentioned herein and not in connection with any proposed offering of securities or as agent of any issuer of any securities. None of BofAS any of its affiliates or their research analysts has any authority whatsoever to make any representation or warranty on behalf of the issuer(s). BofA Global Research policy prohibits research personnel from disclosing a recommendation, investment rating, or investment thesis for review by an issuer prior to the publication of a research report containing such rating, recommendation or investment thesis.

Any information relating to the tax status of financial instruments discussed herein is not intended to provide tax advice or to be used by anyone to provide tax advice. Investors are urged to seek tax advice based on their particular circumstances from an independent tax professional.

The information herein (other than disclosure information relating to BofA Securities and its affiliates) was obtained from various sources and we do not guarantee its accuracy. This information may contain links to third-party websites. BofA Securities is not responsible for the content of any third-party website or any linked content contained in a third-party website. Content contained on such third-party websites is not part of this information and is not incorporated by reference. The inclusion of a link does not imply any endorsement by or any affiliation with BofA Securities. Access to any third-party website is at your own risk, and you should always review the terms and privacy policies at third-party websites before submitting any personal information to them. BofA Securities is not responsible for such terms and privacy policies and expressly disclaims any liability for them.