

OECD public consultation meeting: Amount A of Pillar One

13 September 2022

In brief

The OECD's public consultation on the Progress Report on Amount A of Pillar One ('The Progress Report') was held on 12 September 2022. This alert provides an overview of the consultation meeting and some initial observations.

The OECD previously released the [Progress Report on Amount A of Pillar One](#) on 11 July 2022, with comments due 19 August 2022. The Progress Report contains design rules for different building blocks relating to the new taxing right under Amount A. These rules include proposals, seen for the first time, for the marketing and distribution safe harbour (MDSH) and the elimination of double tax. They also include updates to rules on other building blocks based on previous consultations.

The public meeting provided insights from the OECD and the Task Force on the Digital Economy (TFDE), as well as panels representing a range of views from those who submitted written comments on the Progress Report.

In detail

Overview

The public consultation on the Progress Report follows the OECD's receipt of comments on both the policies and operational execution of various building blocks in Amount A. The OECD received 72 submissions amounting to over 700 pages, two-thirds of which were submitted by businesses and/or their representatives. Developing countries and non-profit organisations had significant representation both in the comment letters and at the consultation.

The discussion at the public consultation focused on the MDSH and the elimination of double taxation (also generally referred to as the rule that determines who pays Amount A). The comments from developing-country stakeholders suggest that if some aspects of these rules do not change course, there could be a collapse in negotiations, potentially resulting in unilateral measures.

Notwithstanding this, OECD and TFDE officials recognised the importance of stakeholder input and highlighted the wide range of support for Pillar One at a high level. OECD and TFDE officials recognised the importance of

eliminating unilateral measures and conceded that more work needs to be done in key areas to meet the intended deadline of mid-2023 for signing the Multilateral Convention (MLC) that will implement the building blocks.

OECD officials noted that the Inclusive Framework (IF) is working on and will soon release revised rules on tax certainty and proposed rules on administration and removal/identification of unilateral measures for public consultation. Several stakeholders expressed hope that the complete Amount A package would then be put out for consultation, as well as draft MLC instrument language.

Observation: Several OECD officials pointedly distinguished ‘different types of complexity,’ including political, operational, formulaic, and technical complexity. In the OECD’s view, it is important for stakeholders to distinguish these different types of complexities in the Amount A dialogue. Therefore, while the OECD accepts that there is conceptual complexity, they appear to believe that there may be less operational complexity (i.e., data gathering, tax calculations, filing, etc.).

Marketing and distribution profit safe harbour

The MDSH clearly remains one of the most controversial areas in the Amount A framework. The two largest themes coming from the consultation were that (1) the MDSH policy is misaligned with the operational execution of the formula; and (2) the factoring of withholding taxes is a critical yet divisive issue.

Business stakeholders echoed their support for including withholding taxes in the calculations and for a ‘domestic (or autonomous) business exemption.’ Representatives from the South Centre and the Trade Union Advisory Committee (TUAC), on the other hand, strongly suggested that including withholding taxes would be a ‘deal breaker’ and spur the uncoordinated implementation of unilateral measures. Consistent with the comments received on the Progress Report, virtually all panellists were critical of the return on depreciation and payroll metric (RoDP) for the MDSH, given that this multiplier likely would not accurately reflect all costs. (There was also ample criticism of the ‘Y’ percentage - representing the portion of a jurisdiction’s residual profits that is eligible for offset under the MDSH - including that it should be taken out of the equation.)

The OECD acknowledged that there is disagreement within the IF on the appropriate metric to use for determining the MDSH, the amount (if any) for the ‘Y’ percentage, and whether withholding taxes should be taken into account.

Elimination of double taxation with respect to Amount A

While recognising that the proposed rules for eliminating double taxation are convoluted, the OECD stated that they are the byproduct of heavy political negotiations and represent a series of compromises among IF delegates. The OECD noted that the RoDP metric was proposed because many delegates believe it is an appropriate indicator for determining a return on substance (i.e., capital and labour). The OECD also noted that commentators criticised the use of RoDP because some groups are more asset or labour intensive than others. The OECD rebuffed these arguments, stating that the RoDP does not discriminate against asset or payroll-heavy groups because the RoDP is measured against the group itself, with no comparison to other groups. Some panellists pointed out that it was strange in our ‘digitalised’ age to completely exclude intangibles from any formulation of ‘substance.’

Various business stakeholders agreed that a formulaic solution for the elimination mechanism was possible but insisted that some of the formulaic complexities require more attention. For example, the tiering ‘waterfall’ approach could lead to distortions and double taxation. Some stakeholders also urged that an exemption (rather than a credit) mechanism be granted explicitly in the MLC to avoid double taxation. Which specific entity should come forward and pay the tax is also a continuing issue of concern for countries.

Observation: The mechanics of the rules surrounding MDSH and the elimination of double tax remain highly complex. Stakeholders are looking for a resolution of anomalies and inconsistencies with the policy intentions that

are materialising, especially as businesses are starting to model these provisions. The importance of offering an effective and timely means of elimination was clear.

Observation: There appear to be different views among the OECD and business stakeholders on whether the reliance on the RoDP approach is agnostic to industry or certain types of business models. Several stakeholders raised issues with respect to potential distortions that the RoDP could create, depending on the group composition on a consolidated basis. For example, an investment hub that is a relieving jurisdiction for a market in which it is not providing services creates a distortion, according to a panellist when pressed by the OECD for a specific example of a disconnect. The OECD appeared receptive to understanding such distortions and disconnections.

Other selected issues (scope, revenue sourcing, tax base)

Stakeholders continued to urge simplification on key building blocks, including scope, revenue sourcing and tax base.

With regard to revenue sourcing, several stakeholders expressed concern regarding the complexity of the information-gathering process and adaptation to new sourcing rules. Some stakeholders asserted that the practices in the ordinary course of business and existing internal controls should govern. They also requested incorporation of more examples directly into the MLC rules/commentary. This could demonstrate how to apply practical solutions to more challenging facts. The OECD and TFDE delegates responded that they have considered the comments and will address the need to make the revenue-sourcing rules more reliable and practicable.

One business spokesperson expressed concern about profit shortfalls and losses, and the resulting distortions caused by a lack of alignment of economic ownership and the designated relieving jurisdiction in some cases. Similar concerns were expressed with respect to the treatment of asset acquisitions, withholding taxes and entities with minority ownership interests. The OECD acknowledged that more input was welcome on the minority shareholders' concerns. Regarding the profit shortfalls and losses, the OECD suggested that the averaging mechanism would address some of these concerns, but acknowledged that more work was needed in these areas.

The OECD commented that the process of refining the revenue-sourcing rules has been a 'journey' and that there still is a significant path ahead with respect to these rules.

Although not specifically on the agenda, the OECD commented that the stability of the tax certainty system is critical to the success of Pillar One.

Observation: The OECD clarified that they were considering a larger scope of issues than were actually being addressed in the consultation. However, it is apparent that the OECD appears to be prioritising the MDSH and elimination of double tax provisions as they are raising the most complexities and anomalies.

Unilateral measures

Regarding the withdrawal of digital service taxes and relevant unilateral measures, various stakeholders expressed concerns regarding an ambiguous or narrow definition of these measures opening the door for potentially widespread promulgation of similar measures undermining Pillar One. Some stakeholders suggested that the definition of relevant similar measures needs to be robust and suggested that the OECD address the treatment of certain grey areas, like diverted profits tax.

The takeaway

The consultation process demonstrated that business still has many serious concerns, including complexity and the arbitrary nature of several of the formulas, but it does seem that the OECD is taking stakeholder comments seriously. The OECD has a continuing urgency to move the project forward to its estimated completion date in mid-2023, but time will tell how realistic that is. Taxpayers should continue to model the provisions and engage with government and business organisations to achieve more simplicity and manageability in the final set of rules.

Let's talk

For a deeper discussion of how the proposed approach to Amount A might affect your business, please contact:

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