BUSINESS at OECD

January 20, 2023

To: Tax Treaties, Transfer Pricing and Financial Transactions Division
Organisation for Economic Cooperation and Development
Centre for Tax Policy and Administration
2 rue André-Pascal
75775, Paris, Cedex 16, France
Submitted by email: tfde@oecd.org

Re: *Business at OECD* (BIAC) comments to OECD's Public Consultation Document "Pillar One – Amount A: Draft Multilateral Convention Provisions on Digital Services Taxes and other Relevant Similar Measures"

Dear Secretariat Team,

Thank you for the opportunity to comment on the public consultation document "Pillar One – Amount A: Draft Multilateral Convention Provisions on Digital Services Taxes and other Relevant Similar Measures" (the "Document"). The *Business at OECD* (BIAC) Tax Committee supports the work undertaken to date by the OECD Secretariat in developing this proposal and the wider Pillar One proposals.

We recall that the principal objective of the two-pillar solution is to restabilize the international tax system, including through the removal of digital services taxes. In October 2021, the Inclusive Framework (IF) reached agreement on a commitment[1] to "*remove all Digital Services Taxes and other relevant similar measures with respect to all companies, and to commit not to introduce such measures in the future*". The objective of these proposals was also to avoid the imposition of other retaliatory measures (e.g., trade and other commercial sanctions). As this is an important political goal, we believe that a statement clearly expressing this objective should be included either in the final text or in the recitals of the Multilateral Convention provisions on digital services taxes and other relevant similar measures.

The OECD identified in its Economic Impact Assessment[2] that, in the absence of such an agreement, there is a concern that tax and trade disputes could reduce global GDP by more than 1%. We agree that this threat is real, and that the work being undertaken by the OECD Secretariat is valuable and we appreciate the continued efforts and resources being dedicated to this project. However, as we note below, in its current stage of development and given the lack of important details, we are not able to (fully) assess whether the Multilateral Convention (MLC) will be effective in this respect.

**Comments on the Document**

We recognize and appreciate that the Secretariat is engaging with stakeholders and that this public consultation has been "*organised in the interest of transparency and consistent with the approach taken*

[1] *Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy*, OECD/G20 Inclusive Framework on BEPS, 8 October 2021.
[2] *Tax Challenges Arising from Digitalisation – Economic Impact Assessment*, OECD/G20 Inclusive Framework on BEPS, 12 October 2020.

*for the other building blocks of Amount A".* However, it seems clear from the text released that this proposal lacks consensus and is still the subject of significant levels of negotiation. In particular, this is apparent on page 3 of the Document where it is stated in bold that:

> ***"The proposals included in this consultation document have been prepared by the OECD Secretariat, and do not represent the consensus views of the Inclusive Framework, the Committee on Fiscal Affairs (CFA) or their subsidiary bodies."***

A number of footnotes are also included throughout the Document, with significant caveats included which cover key aspects of the proposal. This makes it challenging to provide detailed feedback. We would welcome the opportunity to engage further with the Secretariat as the proposals develop and the final design of other important aspects of Amount A becomes clearer. We believe that additional consultation with the business community will be essential in due course.

However, we have highlighted some comments and concerns regarding the apparent direction of travel of the existing proposals, below, which we believe warrant consideration now:

1) ***Definition of digital services tax or relevant similar measure:*** Our members have raised concerns – particularly in the absence of further detail in the Annex of existing measures – that the proposed definition in the Document could potentially result in a number of existing digital services tax being retained. We are also concerned that new measures could be introduced which, while highly "relevant", would be excluded from the scope of the definition. This would significantly undermine the goal of stabilizing the international tax system. It is also likely to place significant pressure on the IF being able to reach agreement on which measures should be included in the Annex.

   In particular, we have the following specific comments in relation to the current definition:

   *Ring-fencing to foreign and foreign-owned businesses*

   The current definition in Article 38(2)(b) requires that the tax is ring-fenced to foreign and foreign-owned businesses or is applicable in practice exclusively or almost exclusively to these businesses. Our members have noted, for example, that digital service tax proposals in EU Member States would not be limited to foreign businesses, as to do so would likely be contrary to EU law. In addition, the "exclusively or almost exclusively" standard must be broad enough to effectively deter discriminatory policies. We believe that this should not be narrowly defined, enabling a small number of local examples to be used by a jurisdiction to justify measures being applied whose overall impact is discriminatory against foreign-owned businesses. For example, the targeted nature of the United Kingdom's digital service tax was highlighted recently in a report by the UK National Audit Office,[3] which stated that 90% of the revenue raised by the UK digital service tax was paid by five businesses.

   In our view, the rule in Article 38(2)(b) should also not apply differently to jurisdictions where there are no residents supplying comparable goods or services, as suggested in footnote 9. In fact, we believe that such a rule against de facto discriminatory taxes would be even more important in situations where a jurisdiction intends the burden of the tax to fall exclusively on

[3] Investigation into the Digital Services Tax - National Audit Office (NAO) report.

foreign businesses. The introduction of a standard of comparability for businesses will add substantial controversy and disputes will inevitably arise from subjective comparability rules. It is also foreseeable that jurisdictions could try to avoid these guardrails and implement discriminatory practices by asserting that there is no comparability with local businesses.

*New nexus standards*

An area of concern for our members is the proliferation of new nexus standards from a corporate income tax perspective (e.g., the introduction of "significant economic presence" tests) that are inconsistent with the OECD Model Tax Convention. Based on the proposed wording of Article 38(2)(c), it appears that these measures would still be permissible as the measures are treated as an income tax under domestic law. Compliance with significant economic presence tests can require significant resources and their de-stabilizing effect is similar to digital services taxes. We would therefore recommend that significant economic presence taxes are treated as a relevant similar measure, otherwise that might lead to a de facto expansion of an Amount A concept to many businesses well outside the scope of Amount A.

*Artificial structuring*

The proposed text of Article 38(3)(a) includes a carve-out for digital services taxes or other relevant similar measures that *"address artificial structuring to avoid other traditional permanent establishment or similar domestic law nexus requirements that are based on physical presence"*. Based on this provision, it seems likely that existing measures (e.g., the UK diverted profits tax) would not currently be in-scope of the MLC. We believe that this leaves open the door to constructing new taxes, which together with the failure to completely remove existing taxes designed to circumvent tax treaties, would materially impede efforts to re-stabilize the international tax system.

*De minimis measures*

Exceptions for "de minimis" measures ignore the destabilizing impact of market-based taxes (e.g., user or end-consumer location), given the substantial data and compliance requirements to support and audit these taxes. Similarly, exceptions for per-unit or per-transaction taxes, or for any ad valorem taxes (as suggested in footnote 11) would, in our view, be inappropriate if they are designed to have a discriminatory effect.

While we appreciate that the footnotes clarify that work is ongoing in relation to a number of aspects of the definition, we believe that it will be crucially important to ensure, via the operation of the MLC, that adjustments to local legislation cannot be made or new legislation introduced which result in measures falling outside the scope of the proposed provisions of the MLC.

We also believe that digital services taxes or relevant similar measures introduced by subnational jurisdictions should be covered by the proposed definition in Article 38.

2) ***Treatment of withholding taxes***: On page 2 of the Document, it is stated that it "*should be noted that measures that are not considered digital services taxes may nevertheless impact Amount A allocations, for example through the operation of the MDSH or the elimination tax base*". While we

appreciate that work remains ongoing regarding the treatment of withholding taxes for Amount A purposes, we note that agreement has not yet been reached.

In our view, it is important that the treatment of withholding taxes is adequately addressed in the MLC. If withholding taxes are not included within the scope of the MDSH in Amount A and were also to fall outside the definition of a digital service tax or relevant similar measure, this could lead to digital services taxes being replaced by increased levels of withholding tax which would undermine the effectiveness of the Pillar One package of proposals and result in additional layers of double taxation for business.

Our preference would be for withholding taxes to form part of the MDSH. Where delegates are not able to reach agreement on this politically, consideration could be given to the inclusion of withholding taxes as a relevant similar measure, to ensure that the risk of double taxation can be minimized for MNEs. In this regard, any increased application or expansion of withholding taxes introduced after a particular date (e.g., 8 October 2021[4]) should be considered to be a relevant similar measure and treated in the same manner as a digital service tax.

Our understanding is that where a digital service tax or relevant similar measure is retained or introduced, Article 38(1) would result in a denial[5] of Amount A allocations being applied on a jurisdictional basis. We agree that this approach is important factor for stabilizing the international tax system, as it provides an incentive for jurisdictions not to retain or impose measures on a unilateral basis.

If it is not possible to treat an increased application or expansion of withholding tax in the same manner as other relevant similar measures, consideration could be given to treating this withholding tax as being creditable for Amount A purposes. However, where this approach is taken, we believe it would be necessary to ensure that stability is still provided for taxpayers that do not come within the scope of Amount A. This may require that the additional withholding tax is treated as (i) being creditable for in-scope taxpayers for Amount A purposes and (ii) falling within the scope of Article 38 if imposed on non-Amount A taxpayers.

The definition of what qualifies as a withholding tax for this purpose could leverage the provisions of the OECD Model Tax Convention[6].

We believe that consideration should also be given to including Article 38(1) assessments within the scope of the proposed Advance Certainty Process for Amount A. Where jurisdictions have a digital service tax or relevant similar measure in place, this will feed into an MNE group's allocation of profits to market jurisdictions. We believe that being able to clarify which jurisdictions qualify as market jurisdictions during the Advance Certainty Process would be helpful from a tax certainty perspective.

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[4] We have selected this date as it reflects the date on which the political commitment was provided not to impose digital service taxes or relevant similar measures, as part of the Inclusive Framework *Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy*.

[5] We note that whether the denial is full or partial is still under consideration. In our view, a full denial would be preferable for simplicity and to disincentivize the application of unilateral measures.

[6] Model Tax Convention on Income and on Capital: Condensed Version, OECD, 2017.

3) ***Interaction with other aspects Pillar One Amount A:*** We note the comment in footnote 4 of the Document that the provisions eliminating Amount A allocations – where a digital service tax is retained or introduced – are still under development. In our view, it is important that, at a minimum, the final design of the mechanism minimizes the risk that businesses suffer double taxation, and as with all other currently undecided items, we hope there will be another opportunity for stakeholder input before the final MLC is released.

   Footnote 2 also states that consideration is being given *"to whether any existing measure could continue to be applied against an MNE with a UPE located in a jurisdiction that is not Party to the MLC"*, and whether it would be possible for a jurisdiction to introduce future measures against MNEs that have a UPE located in a jurisdiction which is not a party to the MLC**.**

   Depending on which jurisdictions ultimately sign the MLC, this potentially could also significantly expand the impact of digital services taxes on MNE groups. More generally, this also raises a question of how Amount A of Pillar One is intended to operate if a UPE is based in a jurisdiction which does not sign-up to the MLC, but has operations in other jurisdictions that have signed up to implement Amount A. It is not clear to us currently whether that MNE group would then be out-of-scope of Amount A, if reallocations of profit could still be required, and how these would be applied in practice.

   We understand that Amount A is not intended to come into effect until a critical mass of jurisdictions have committed to ratifying the MLC and we therefore appreciate that this point may be clarified in due course. In our view, it truly will be important that this point is clarified.

   It is important to recognize the starting point for this project – jurisdictions are in good faith attempting to ensure the stabilization of the international tax system. However, footnote 4 risks setting up a choice among (i) jurisdictions that sign-up to the MLC and eliminate these measures and (ii) jurisdictions that do not sign-up and introduce or retain such measures. This would seem to be contrary to the overall objective of the project, and we believe that the position of the IF should be to encourage all jurisdictions to eliminate destabilizing measures irrespective of whether or not the jurisdiction has decided to ratify the MLC.

We thank you for the opportunity to comment and hope that a further opportunity will be provided to do so again when the project is further advanced. We would be pleased to respond to any questions arising from our general and specific comments provided and would also welcome any opportunity to work with you and the TFDE in order to further progress the development of this important project.

Sincerely,

Alan McLean
Chair, *Business at OECD* (BIAC) Tax Committee

William H. Morris
Chair Emeritus

Cc: Hanni Rosenbaum, Executive Director, *Business at OECD* (BIAC)

## Appendix I

## Key Features of a Digital Service Tax or other Relevant Similar Measure

**Issues for consideration**

1) The definition of a digital service tax and relevant similar measure should be as broadly defined as possible.

   It could include conditions that cover measures that:

   a) impose taxation based on market-based criteria

   However, condition (a) would not apply when it is sufficiently clear that:
   - i) the measure applies across business models and does not attempt to ring-fence the digital economy (or any other specific sectors/ business models);
   - ii) will apply equally to both foreign-owned companies as well as domestic resident businesses; and
   - iii) is not applicable exclusively or almost exclusively to non-residents or foreign-owned businesses in practice.

2) The definition and provisions should also be forward-looking (i.e., the risk of the focus being shifted from digital service taxes to other types of taxes should be mitigated where possible).

3) The intention should be to improve tax certainty and limit disputes over whether the conditions of a measure introduced result in it being in the scope of the MLC.

4) Safeguards introduced should be designed to prioritize the long-standing tax policy of avoiding the risk of an MNE being subject to double taxation (e.g., the retention of digital services taxes and relevant similar measures should disapply Amount A allocations). Any taxes that remain permissible under this framework should be the type of taxes against which countries would introduce measures (e.g., credits or exemptions) to ensure relief from double taxation.[7]

[7] As an example, the United States has indicated in the preamble of recent regulations governing foreign tax credits that it would re-visit the regulations in response to the Pillar One rules. We recommend that countries, including the US, ensure resolution of double taxation by providing credits (or exemption) for any taxes deemed permissible (i.e., outside the definition of a digital service tax or relevant similar measure) to ensure this long-standing policy goal is maintained.