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“OECD Blueprint on Pillar One Solutions”

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About BEPS 2.0

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Background

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BEPS Action 1 - OECD/G20 Proposals per October 2020:

- **Pillar One**: profit allocation and nexus rules
  to allocate more taxing rights to markets (source countries)

  and in parallel

- **Pillar Two:**
  Proposal for a **globally imposed minimum tax**, which according to the OECD does not require a significant number of countries to agree

- More than 100 countries participating in BEPS 2.0 through the "**Inclusive Framework**"

Pillar 1 - Status quo ante (2019)

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The Secretariat's proposal for a Unified Approach (Pillar One);
i.e. the search for a minimum consensus to achieve unanimity ("*level playing field*")

- **Amount A (new taxing rights):**
  Creation of a **new nexus rule**, in the context of which "**deemed residual profits**", will be taxed in accordance with "**formulary approach**" ("**FA**") methods;
  new stand-alone treaty provision, not dependent on physical presence and based largely on **in-country sales**

- **Amount B (no new taxing rights):**
  Distribution functions taxed according to existing rules, thereby maintaining the "arm's length standard", ("**ALS**")

- **Amount C (no new taxing rights)**
  Any dispute between the market jurisdiction and the taxpayer over any element of the Proposal should be subject to legally binding and effective **dispute** prevention and **resolution mechanisms**

Pillar 1 - Status quo (2020)

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Steering Group for the Inclusive Framework; Pillar One Blue Print

- **Amount A (new taxing rights):**
  Basic distinction between Automated Digital Services (“**ADS”**) and Consumer Facing Business (“**CFB**”)

- **Amount B (no new taxing rights):**
  Related party distributors that perform “baseline marketing and distribution activities” in a manner that is aligned to arm’s length principle (“ALP”)

- **Building Tax Certainty**
  To provide tax certainty for and beyond Amount A
  Refurbish MAP and introduce mandatory dispute resolution mechanisms.

Nexus Rules

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Will apply differently to ADS and CFB (214)

- **Automated Digital Services** (ADS)
  Exceeding a given **revenue threshold** in the market jurisdiction
  is the only test necessary to establish **nexus** => sales exceeding [EUR 1.0] Mio. p.a.

- **Consumer Facing Business** (CFB)
  Sales exceeding [EUR 3.0 Mio] p.a. and either
  a physical presence (subsidiary or PE) in the market jurisdiction, **or**
  sales exceeding EUR [15 to 20 Mio.] p.a. which are **deemed to create a presence beyond mere sales** (216)

Source Rules

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In order to allocate income to a particular market (source country), one has to determine the source of that income

A) General Rule

- Unlike the traditional source rules, which differentiate between local income and foreign source income, here we look for **multilaterally applicable source r**ules

- Define what kind of business is typically earning income (e.g. online advertising services) and look for the corresponding revenue sourcing rules (e.g. revenue from online advertising services) that will apply **to each separately identifiable revenue stream** (262)

Source Rules

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B) Automated Digital Services

Basic source rules not applying the 50 : 50 revenue split between the seller and the purchaser

- Revenue from online advertising services is based on the real-time location of the viewer

- Revenue on online advertising services not based on the real time location of the viewer is based on the ordinary residence of the viewer as further specified by relevant indicators

- Revenue from the sale of other alienation of user data not based on the real time location of the user are located at the ordinary residence of the viewer, as further specified by relevant indicators

Basic source rules also being used as cross reference for other types of income such as e.g.

- Revenue **from online search engines** using either the "*revenue from online advertisement services*" or the "*revenue from the sale of other alienation*" source rule

Source Rules

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B) Automated Digital Services (continued)

The revenue is sourced based on a 50 : 50 split between the seller and the purchaser (278) => there is a hierarchy of different source rules applicable to either purchaser or seller

- **Purchaser of Goods** : Ordinary residence of the purchaser as further specified by **relevant indicators** (such as e.g. delivery address of the purchaser etc.

- **Seller of Goods:** Ordinary residence of the Seller as specified by relevant indicators (such as e.g. the jurisdiction of the Seller's principal place of business etc.

- **Purchaser of Services**: realtime location of the Purchasers as further specified by relevant indicators (such as e.g. geolocation of the device used by the purchaser etc.

- **Seller of services**:
  Jurisdiction where the service is being performed

Source Rules

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C) Consumer Facing Business

- Revenue from **goods sold directly** to customers:
  place of final delivery as further specified by “relevant indicators”

- Revenue from goods sold through an **Independent Distributor**:
  place of final delivery, as further specified by “relevant indicators

- Revenue from consumer facing **services**:
  place of enjoyment or use of the services, i.e. the address where the service is performed (?)(309)

Source Rules

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C) Consumer Facing Business (continued)
Revenue from franchising goods or licensing intangibles:
distinguishes between consumer facing goods and consumer facing services

- Goods: Place of final delivery of the goods
- Services: Place of enjoyment or use of the service (312)

Avoiding Double Taxation

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Amount A will apply as an overlay to the existing, ALP based profit allocation rules

- A mechanism to reconcile the new taxing rights and the existing profit allocation rules (calculated on an entity basis) is necessary to prevent double taxation

- In order to do so there is a complicated four step process allowing to identify the paying entities, which will be put in place.

Determining the Tax Base

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Tax Base => Net PBT of the Consolidated Accounts of the UPE

- **Determine Accounting Systems: IFRS, GAAP, others**
- **Using segmented accounts (business lines or geographical basis)**
- **Loss carry forward rules**

Determining the Tax Base

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Profit based approach equals profit margin based approach (579)
Here: Profit based approach (583)

- Determine “residual value” (W) by adjusting PBT with a factor “revenues times assumed profitability threshold, e.g. 10%
  PBT **6’000**
  Revenues 25’0000
  (assumed **profitability threshold** 10%)
  W = 6’000 * (25’000 times 0.1) = **4’000**

- Determine taxable income (quantum) by multiplying W with an assumed amount A **reallocation percentage** (e.g 20%)
  W * 0.2 = **800**

- Allocate (800) to the relevant markets/segments
  as a percentage of total revenues

Tax Certainty – Accounting Issues

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Request for Tax Certainty launched by MNE groups

- Requests for “**early certainty**” (i.e. before any audits took place) submitted by the groups coordinating entity to its **lead tax administration**, usually (but not necessarily!) the tax administration of the UPE (753)
- are subject to MNE providing an agreement signed by all constituent entities (754) and
- can lead to the establishment of a **panel of tax administrations**

DTC MAP - Mandatory Arbitration

2019: A procedure between the competent authorities involved

Preparing "Terms of Reference" and choosing between two methods

Final offer arbitration (FOA)
(base ball arbitration)

Independent opinion arbitration

«Blueprint» Determination Panels

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Ongoing technical work is addressing the relationship between the determination panel and the existing mandatory binding dispute resolution mechanisms (823)

- Decision of the determination panel would generally also be binding on the competent authorities (826 on page 208)

Pillar 1 – Political Agenda

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On June 12, 2020 U.S. Treasury Secretary Mnuchin informed the finance ministers of France, Italy, Spain, and the United Kingdom in writing that the United States is calling upon the OECD "to **pause** discussions on Pillar 1, with a view towards resuming them later this year"

- If the government continues (with a majority in both houses) the U.S. could be rejoining the discussions, If there will be a new government, Pillar I discussions will (as far as the U.S. are concerned) restart from scratch.
- **The more than 100 countries supporting the OECD's Inclusive Framework want to go ahead and finalize the BEPS 2.0. Pillar One Project (realize a consensus based solution by the end of 2020)**
- Daily Tax Clip, October 8, 2020 **"They are worried the OECD won't be able to pull this off because the U.S. has been back and forth on its position"** (Kate Barton, EY Global Vice Chair of Tax)
- The EU MS will continue to implement the DST on a country by country basis

Thank you for your attention !