THE 100 GROUP

Taxation Committee

Tax Policy and Statistics Division
Centre for Tax Policy and Administration
OECD

11 November 2019

By email: TFDE@OECD.org

Dear Sirs

OECD Public Consultation Document: Secretariat Proposal for a "unified Approach' under Pillar One

We welcome the opportunity to respond on the OECD's public consultation document on a 'Unified Approach' under Pillar One.

The 100 Group is a representative body made up of large UK businesses from a variety of sectors and as such the implications of the proposals and the relative concerns of our members will vary.

We set out below our comments on the proposals in areas where we believe there is a broad consensus across our membership. In responding we would also acknowledge the response of the CBI in the UK which many of our members will have contributed to and which we also support.

Summary comments

We recognise that the digital economy and how it is taxed is of concern to governments around the world and this has led to a proliferation of unilateral and uncoordinated measures. The work the OECD is undertaking to move forward on an international consensus solution is vitally important. We recognise the need for taxpayers and governments alike to arrive at a workable solution as soon as possible.

At section 2 of the Secretariat's Proposal, the OECD document sets out points of commonality across the three alternative Pillar One proposals as set out in the Programme of Work. The last bullet states that all options search for simplicity, stabilisation of the tax system, and increased tax certainty in implementation.

Most businesses view these features as critical to any workable solution and view the following as key requirements whatever solution is finally proposed:

- Profits (and not revenues) should be taxed once and only once. Beyond this, however, most businesses will generally be agnostic as to where they pay the tax.
- The proposals reallocate profit to market or destination jurisdictions but they must also ensure an equal and opposite reduction in profit in the 'source' jurisdiction.

- Any new proposals should seek to reduce and simplify compliance burdens as much as possible and offer increased certainty as a key outcome for MNEs.
- The proposals offer scope for less controversy in some areas but will produce new controversy in others. Generally there will be less control over where taxes are paid and for this reason a robust, mandatory and binding dispute resolution process will be very important.
- Agreement to repeal any unilateral measures as well as to relinquish taxing rights on profit reallocated to market jurisdictions must be required from all countries that agree to move forward with any OECD framework.
- Any solution should not act as a barrier to trade or to economic decisions. It must make sense for large and small economies.
- Any Pillar One solution should not be agreed without an agreed approach for Pillar Two also. Inevitably there will be an interdependence and the two proposals should work together to produce an outcome that is fair and appropriate.

We find the suggestion of various interested parties to set up a "One Stop Shop" to oversee this regime very compelling as it would enable many of the above criteria to be met in an efficient manner. In particular, some form of "One Stop Shop" or centralised agency would provide the following benefits:

- Allow the proposals to be designed in detail on a centralised basis which would not only help consistency of approach but would also make the proposals as a whole more attractive for smaller economies.
- It would allow a mechanism for centralised filing and payment with a return filed in the location of the parent and the central agency dealing with reallocations and payments.
- It would offer a more efficient centralised binding dispute resolution process which would ensure that the principles and procedures of dispute resolution frameworks are applied consistently and equitably.
- It would ensure that profit allocated to market jurisdictions is matched by a profit reduction in the other relevant countries on an equitable basis and it could ensure that profit is only allocated to jurisdictions that sign up to the binding resolution process.
- It would provide consistency of approach and application, reducing the ability of different jurisdictions to take unilateral approaches that destroy the cohesion of international taxing frameworks.

More detailed comments

Scope

The final scope of the approach, together with its rationale for excluding or including particular business models, should be grounded in a clearly articulated policy rationale.

Key to defining scope will be drawing definitions and limitations clearly. There are still many moving parts such as whether specific industries should be excluded, to what degree the rules

should look through third party distributors and how to deal with multiple components in the value chain etc.

Given that the current scope is very broadly defined (all large consumer-facing businesses), many business models should not clearly fall within defined parameters. Consideration should be given to supplementing clear rules with a principles based approach which will help drawing conclusions at the margins. For example, should exemptions exist for companies which make routine profits, do not project themselves into the daily lives of users, or which generate all revenues in the market jurisdiction (rather than remotely or via marketing and distribution structures)? Other industries are prohibited from being consumer facing due to regulation and it is important that economically relevant characteristics of an industry or business model are considered in determining whether they are in our out of scope.

As far as possible use should be made of existing well-understood and widely adopted definitions and reporting structures to minimise additional compliance burdens. For example, the definition of the MNE group could be aligned with international accounting rules.

The policy principles must be sufficient to cater to business models of tomorrow as well as today to ensure the proposals are sustainable and do not require constant redrafting and updating.

Nexus

The nexus proposals rely on sales or revenue. However many MNEs may not currently track consumers on a geographical basis. As a result MNEs will need to implement new and costly systems to ensure compliance with any proposal. Not only will these take time to implement and embed but they can only be commissioned once there is a clear set of rules on which to base any systems requirements.

In relation to questions of defining and applying country specific sales thresholds, the nexus proposals need to define the appropriate metric or data points. Consistent sales recognition may be subjective as different entities within an MNE group may recognise and account for sales in different ways which could potentially distort the threshold.

In relation to both the application of sales thresholds and ensuring that smaller economies can benefit, we think that a more centralised approach such as a “One Stop Shop” would be beneficial. The centralised approach could ensure that smaller economies are appropriately catered for, minimising their own costs of administering the new regime.

Care will be needed that the introduction of these rules do not generate unhelpful behaviours or responses from either taxpayers or governments which would distort outcomes and hamper implementation of these proposals For example, any nexus that arises as a result of these proposals should not result in countries arguing taxing rights also arise for other taxes. Similarly, a reallocation of profit to market jurisdictions should not be used to argue that exit taxation arises in the country from which the profit is reallocated.

Calculation of group profits for Amount A

As highlighted above, we consider it is important that existing and well-understood reporting systems are used whenever possible. Therefore a starting point for group consolidated profit

as calculated and reported under existing international accounting standards would seem appropriate. However, considerations should be given as to what adjustments may be necessary to such a measure.

Standardised adjustments should be kept to a minimum to increase transparency and reduce complexity. However, we do think that removal of exceptional items should be allowed so that reallocations are operated on a 'business as usual' profit figure. This may include profits or losses on disposal, restructuring costs, amortisation of IP not relevant to the activities of the market jurisdictions, and impairments or fair value movements that do not reflect the underlying performance of the business. Consolidated financial statements seek to reduce differences in accounting profit arising from different transaction structures (eg shares deals compared to asset deals) and consideration to how these should be dealt with will be needed.

Large businesses are required to report segmental information as part of their financial statements and they will also often report internally on a segmented basis for management accounting purposes. A segmented approach is much more likely to allow accurate reflection of material differences in profitability across specific regions and business lines.

We consider that it should be possible for authorities to place reliance on an MNE's existing segmental reporting as this is generally part of an MNE's reporting for regulatory and investor purposes. This means that such figures are already materially accurate and subject to external scrutiny.

It should not be possible for one country to override a taxpayer's segmentation analysis without corresponding adjustments being made to other jurisdictions. In practice this would mean that any adjustments to a business' approach to segmentation would need to be overseen centrally, preferably through some form of centralised agency or "One Stop Shop" taxing authority.

It should also be possible for an MNE to proactively document its segmentation approach and agree this with the central agency which, if such agency had the requisite authority, could then bind other jurisdictions into the approach for that taxpayer. This would be a powerful tool in promoting certainty and stability for taxpayers although we accept it may take some time to develop the relevant experience and skills to allow this to happen.

Determination of Amount A

Amount A is determined by excluding deemed routine profits to identify deemed residual profits which are then located to market jusridictions based on agreed allocation keys.

Any approach to the determination of Amount A will need to take into account factors including:

1. Any system will need to recognise that routine profits can vary across business models, even in the same industry sector.
2. Reward must be given for all routine functions on a cumulative basis before determining whether there are any above normal profits to allocate under amount A Some industries, especially R&D intensive ones, will incur significant initial outlays which are highly uncertain and will often have been written off. Returns may take

many years to generate and therefore produce a false appearance of a non-routine return arising.

3. In a similar vein, some R&D projects will never result in any revenue. An approach to dealing with such spend must also be developed. As is acknowledged in the document, it should not be the case that only profitable product lines are subject to reallocation as this would unfairly penalise the 'source' jurisdiction.
4. The mechanism to determine the above normal profits to allocate to markets under Amount A needs to ensure there is an equal and opposite deduction in the source jurisdiction aligned to where residual profit currently arises under the arm's length principle.
5. The mechanism should avoid double counting (eg if a market return is already included within the existing transfer pricing framework a further market allocation may lead to double counting).

Elimination of double taxation in relation to Amount A

As has been mentioned at several other points in this response, in order to facilitate the consistent implementation of any proposal, and to ensure the minimisation of any double taxation, we think that the OECD should consider a centralised agency or "One Stop Shop" to oversee the regime which has the ability to bind both taxpayers and tax authorities.

If this central agency opined on and facilitated any profit reallocation this would also reduce compliance burdens and uncertainty for taxpayers. For example, the parent company of an MNE could make a comprehensive filing with the agency (including setting out the exact legal entities that get relief from Amount A profits reallocated to market jurisdictions) and could make payment to the same agency which would then be responsible for reallocating the profits and the payment to the relevant jurisdiction.

The agency could also ensure that relief is given in an appropriate and proportionate manner (for example, where the original costs rested with multiple entities/jurisdictions).

Any agency could also only allow reallocations of profit to market jurisdictions that have signed up to a binding and centralised dispute resolution mechanism.

Where an MNE has multiple entities in one jurisdiction, we think that the group should be able to nominate a particular entity to receive any adjustments.

Amount B

Most businesses accept there is a trade-off between tax accuracy or purity and administrative ease. On this basis, most of our members think that a fixed percentage based on industry would be sensible. Several members have pointed to the ATO which has something similar.

The interaction of fixed percentages with loss making or low margin returns would need to be considered.

Amount C/dispute prevention and resolution

As previously stated, we consider that many of the challenges that will arise under Amount C and dispute prevention/resolution would be solved if a centralised agency or "One Stop Shop"

was established which had the power to bind taxpayers and authorities alike into a consistent approach.

Such an approach would allow oversight to ensure that the amounts A, B and C interact to produce results which represent fair outcomes for taxpayers and governments alike.

Conclusion

We trust the above comments are useful in developing the proposals further. Should you have any queries or wish to discuss the response please do contact me at chris.oshea@100group.co.uk

Yours faithfully

Chris O'Shea

Chair
Tax Committee

Who we are:
The 100 Group of Finance Directors represents the view of the finance directors of FTSE100 and several large UK private companies. Our member companies represent almost 90% of the market capitalisation of the UKFTSE 100 Index. Our aim is to contribute positively to the development of UK and international policy and practice on matters that affect our business, including taxation, financial reporting, corporate governance and capital market regulation. Whilst this letter expresses the views of the 100 Group of Finance Directors as a whole, those views are not necessarily those of our individual members.