

February 18, 2022

Tax Treaties, Transfer Pricing and Financial Transactions Division
Centre for Tax Policy and Administration
Organisation for Economic Co-operation and Development
By email: TFDE@oecd.org

Re: Business Roundtable comments on OECD public consultation document, “Pillar One – Amount A: Draft Model Rules for Nexus and Revenue Sourcing”

Dear Sir/Madam,

Business Roundtable welcomes the OECD’s commitment to working multilaterally and with the private sector to ensure sound tax policies and straightforward tax administration, which are essential to protecting investment and economic growth.

On behalf of more than 200 Chief Executive Officers of America's leading companies, Business Roundtable is pleased to submit comments in response to the OECD public consultation document, “Pillar One—Amount A: Draft Model Rules for Nexus and Revenue Sourcing,” dated February 4, 2022.

High-level comments

We wish to emphasize at the outset the following internationally accepted tax policy goals, which are the second and third elements in the 1998 Ottawa Taxation Framework:

Efficiency

ii) Compliance costs for taxpayers and administrative costs for the tax authorities should be minimized as far as possible.

Certainty and simplicity

iii) The tax rules should be clear and simple to understand so that taxpayers can anticipate the tax consequences in advance of a transaction, including knowing when, where and how the tax is to be accounted.”

The draft Model Rules on revenue sourcing in the Consultation Document are, unfortunately, not at all clear or simple to understand. Indeed, they have been written in a way that guarantees confusion and problems of interpretation. There are many defined categories of revenue and other defined terms, and each definition gives rise to questions of interpretation and line-drawing. Moreover, some of the defined terms incorporate other defined terms in a way that cannot be reconciled with the standalone definition of the incorporated term (examples are noted in the detailed comments below). In addition, sometimes a word that is a defined term when capitalized (e.g., Location) is used without being capitalized (location), raising the question of whether the latter’s meaning was intended to be consistent with the defined term.

As a result of their lack of clarity and simplicity, the draft rules would produce uncertainty regarding tax results for MNEs and governments alike. For the affected MNEs this uncertainty would be likely to exceed by a large margin the current level of uncertainty arising from existing tax rules, in terms of the scope and frequency of disputes.

In addition, the draft rules would require an enormous amount of time and effort for governments to administer and for in-scope businesses to comply with them. The Consultation Document asserts that MNEs would not have to collect any information beyond what they already collect in the ordinary course of business, but the draft rules call that statement into question. Even if it is true, the draft rules would require in-scope businesses to analyze and manage the information in new and very burdensome ways (discussed further below).

Consequently, the draft rules would fail with respect to the goals of efficiency, clarity and certainty. The very short consultation period of two weeks severely limits the ability of stakeholders to suggest improvements to the draft rules. More time is needed to work collaboratively in an effort to have workable rules on revenue sourcing. Little comfort can be taken from the Consultation Document's many references to forthcoming explanations and clarifications in a Commentary to the Model Rules, as it appears that stakeholders will not have the opportunity to comment on a draft version of the Commentary.

The Inclusive Framework and the OECD should explore the possibility of simplifying these draft rules by taking advantage of the existing international VAT rules in the OECD's International VAT/GST Guidelines. These guidelines are based on the destination principle—i.e., taxation in the jurisdiction of consumption—and are currently used and understood by MNEs and tax administrations around the world.

Detailed comments regarding the substance and effect of the draft nexus and sourcing rules

Nexus: Materiality

The nexus threshold test should be raised to require that revenues of a Covered Group arising in a jurisdiction be equal to or greater than EUR 10 million, indexed for inflation using an index from a company's home country jurisdiction. This threshold would achieve the goal of limiting nexus to cases that are "material" (as stated in the Background section of the Consultation Document). A simple comparison of the EUR 20 billion threshold for groups to be in-scope for Amount A clearly shows that the proposed nexus thresholds of EUR 1 million / 250 thousand are not even close to "material" thresholds.

Sourcing: In General

Very importantly, the most concerning and impractical element of the draft rules is sourcing on a transaction-by-transaction basis, which requires a sub-invoice analysis. The most detailed level of analysis should be at the customer level by legal entity. For this purpose, a customer should be a customer as defined in a company's billing system. Further, requiring ratios based on every type of monetization approach separately is also unrealistically burdensome.

The draft definition of "Reliable Indicator" makes it unclear whether VAT (or other indirect tax) indicators qualify as Reliable Indicators, and seems likely to lead to increased, rather than decreased, controversy. In addition, the stated Reliable Indicators for particular types of revenue require information a company must request from its customers solely for purposes of complying with these model sourcing rules, instead of information a company

would typically collect in the ordinary course of business. The definition should be amended to make it clearer that indicators a company already relies upon for other tax compliance obligations {e.g., VAT on ESS supplied to consumers, or compliance with the U.S. Foreign Derived Intangible Income (FDII) regime} will be Reliable Indicators for purposes of the sourcing rules.

Sourcing: Advertising Services

Regarding advertising services, we have concerns about the granularity of the data required. There is a large amount of data required (clicks and impressions are in the billions), and there are questions about the systems in place to track click-by-click or impression-by-impression data.

A single, uniform approach should be chosen to better ensure availability of data, consistency, and administrability. Specifically, all the locations where ads are shown (impression location) by customer and legal entity should be considered. Because the availability of impression location data may vary across products or customers and change over time in response to regulatory or industry practices, companies should be permitted to use the location data that is available in the ordinary course of business (e.g., device location, IP address location, location based on a combination of indicators / multifactor).

To avoid duplication of compliance requirements, limit unnecessary costs, and reduce needless disputes, there should be a safe harbor for any methodology that establishes impression location in a similar manner to the method required or permitted for any other tax compliance purpose.

Sourcing: B2C/B2B Services

We believe that using VAT indicators would be the best approach to sourcing revenue from these services.

It is overly complicated to distinguish between Consumers, non-Large Business Customers, and Large Business Customers. It may not be possible to discern whether a customer acquires a service for personal purposes rather than for commercial or professional purposes. In some instances, the same customer may acquire the services for both personal and business purposes.

Covered Groups may have many thousands or millions of customers and may not have the ability to see the Country-by-Country reporting obligations of customers (public financial data may not exist or be readily available to a Covered Group). Linking contracting parties to their Parent Company may not be possible (i.e., an affiliate in a jurisdiction may operate under a name unrelated to that of its parent).

Customer-provided headcount should not be required. Customer headcount information is not commercial and does not provide a better answer to the question of where services are used than other information such as VAT indicators. The contracting employee of the Business Customer may not have access to the relevant information or may have valid business reasons for not wanting to share this type of information with the Covered Group.

Taxpayers need some way to have certainty before creating complex systems and processes for this data. For example, it might make sense to have a transition period in which more flexible indicators are allowed or an allocation key can be used, with a process to get

advance certainty on the acceptability of the taxpayer's sourcing methodology before it is required to implement the system.

In this regard, we note that the draft rules state that a Covered Group "must demonstrate that its internal control framework ensures that a Reliable Method is used" in applying the sourcing rules (page 12, paragraph 8). This requirement regarding the existence and effectiveness of an internal control framework for compliance with the sourcing rules goes beyond the need to determine how much of the group's revenue arose in which jurisdictions for the relevant period. Is the design and functioning of the internal control framework a separate issue for governments to audit?

Regarding B2B cloud services, companies may have limited or no data available on the location where a customer uses B2B cloud services. Accordingly, to the extent that taxpayers are required to establish the place of use for B2B cloud services, taxpayers should be permitted to do so using access location data that is available in the ordinary course of business {e.g., location data on where a customer accesses certain cloud service interfaces to prevent fraud or abuse (interface data)}.

As in the case of advertising services, the most detailed level of analysis should be at the customer level by legal entity, where a customer is a customer as defined in a company's billing system. Additionally, there should be a safe harbor for any methodology that establishes location in a similar manner for another tax compliance purpose. To the extent that location data is not available using a methodology covered by the safe harbor, companies should be able to establish location using billing address.

Sourcing: Sales of Finished Goods to Distributors

Sales of tangible property to distributors (B2B sales) should be based on location data of final customers that companies obtain in the ordinary course of business, such as warranty registrations or electronic activations. Companies may not be able to join this location data with revenue data because, for example, this data may not be consumed by billing systems in the ordinary course of business. In that case, companies should be able to use this location data to compute an overall location ratio that can be applied with respect to all B2B sales at the company level instead of the customer level.

The allocation key for "Tail-End Revenues" addresses cases where a taxpayer is unable to gather reliable data about certain sales. While this is helpful, there is a far more compelling issue related to "tail end" revenue, and that is that systems for compliance (in the best of cases) will be expensive and require significant resources. Companies at the scale that are in-scope for Amount A cannot develop systems for every single product in existence without incurring extremely disproportionate costs. Companies should be able to use the customer's billing address as a Reliable Indicator for amounts that represent 10% or less of the company's total revenues from third parties, without first having to consider alternative methodologies of establishing a relevant location.

Moreover, in the ordinary course of business, companies may record certain adjustments to revenue (e.g., certain contra revenue transactions) with respect to no specific customers or transactions. Companies should be permitted to prorate adjustments to revenue that are not recorded with respect to specific customers using a reasonable methodology such as by revenue or product, depending on how these adjustments are recorded in the ordinary course of business.

Sourcing: IP Licensing for Merchandise Related to Marketing of Products and Content

Clarification is needed in relation to the licensing of IP embodied in merchandise related to marketing of the Covered Group's products and services. For example, a motion picture studio may license certain copyrights (characters, names, likenesses, etc.) to a third-party merchandiser to produce and sell promotional products as part of the marketing of the motion picture being distributed by the studio. Similarly, a game developer may license certain copyrights (tradename, logo, etc.) to third-party merchandisers to produce and sell promotional products as part of the marketing of its game console or game content. In the circumstance where the Covered Group is not making the sale of the promotional products directly, there is no "Reasonable Indicator" available, and the sourcing of the license fee revenue should be determined using the Global Allocation Key.

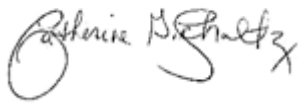
Detailed comments on drafting issues

- On page 13 of the Consultation Document, paragraph B(1) gives the sourcing rule for "Revenues derived from a transaction for the sale of Finished Goods to the Final Customer through an Independent Distributor". The drafting raises the question, what Revenues are covered by this rule? The rule relates to Revenues of a Covered Group. The term Independent Distributor is defined as "an enterprise that is not a member of the Covered Group that distributes or resells the Covered Group's Finished Goods." So a "sale of Finished Goods to the Final Customer through an Independent Distributor" is a sale by the Independent Distributor, and does not necessarily produce any Revenues for the Covered Group. Presumably there are cases in which an independent distributor buys finished goods for an agreed price and takes the risk of not being able to resell the goods at a higher price, as well as cases in which a distributor has bought inventory on this basis and later has had to scrap some of it as unsellable. The sourcing rule in B(1) needs to be rewritten to cover revenue from "the sale of Finished Goods to an Independent Distributor". Compare the drafting of the sourcing rule for sales of components on page 15, Part 4, paragraph A(1).
- On page 13, in the first sentence of paragraph B(4), the words "a transaction for" make no sense and should be deleted. More generally, paragraphs B(3) and B(4) on this page demonstrate the difficulty of reading and understanding these draft rules. It is necessary to spend time looking at the definitions of various terms before one can begin to understand these rules, and even then, it is not at all clear exactly what they mean.
- On page 14, paragraph C and note 18 deal with the sourcing rules for sales of Digital Goods by simply stating that they are the same as the rules for B2C and B2B services (i.e., location of the consumer, and place of use by the business customer). B2C and B2B services are defined at the end of the Consultation Document very generally as services to consumers and services to businesses. Stating the sourcing rules for Digital Goods in that way risks confusion, because there are different sourcing rules for income from B2C and B2B services in other categories such as advertising services, online intermediation services, services connected to tangible property, services performed at the location of the customer, etc. Admittedly there is a reference to the applicable paragraphs of the sourcing rules for services, but it would be better to simply state the sourcing rules for Digital Goods without referring to B2C and B2B services.

- On page 15, paragraph A(4) gives the source rule for income from "Services Performed at the Location of the Customer". This is a defined phrase in which the meaning of the word "location" is inconsistent with the definition of "Location" elsewhere in the list of defined terms. We note that other sourcing rules use the word "place" rather than "location". This category of services would be better named "Services Performed at the Place of the Customer" in order to avoid the conflict of defined terms.
- On page 26, the definition of "Customer" is in conflict with the definition of "Final Customer".
- On page 34, the definition of "Non-customer Revenues" includes "gains on the disposition of assets". This appears to conflict with note 14 on page 12, which says that the Commentary will clarify that revenue from the sale of capital assets will be treated as revenue from the sale of Finished Goods.

Business Roundtable urges the Inclusive Framework to take the above comments into account in its further work on the Pillar One Model Rules, in the interest of aligning the rules with sound tax policy. Thank you for considering our comments and recommendations. We would be happy to discuss these comments or any other matters you believe would be helpful.

Sincerely,

A handwritten signature in black ink, appearing to read "Catherine Schultz". The signature is fluid and cursive, with the first name and last name clearly distinguishable.

Catherine Schultz
Vice President, Tax and Fiscal Policy
Business Roundtable
cschultz@brt.org
+1 202-467-5266.