INVESTMENT COMPANY INSTITUTE

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OECD Public Consultation Document: Proposal for a "Unified Approach" under Pillar One

[32004]

October 10, 2019 TO: ICI Members
ICI Global Members
ICI Global Tax Committee
Management Company Tax Subcommittee
Tax Committee SUBJECTS: International/Global
Tax RE: OECD Public Consultation Document: Proposal for a "Unified Approach" under Pillar One_

The OECD released a proposal for a “unified approach” on the allocation of international taxing rights that draws on the three alternatives (i.e., “user participation,” “marketing intangibles,” and “significant economic presence”) set out in the Programme of Work under Pillar 1.[1]

The key features of the Unified Approach are summarized below.

- Scope. The proposal is not limited to digital companies and focuses on consumer-facing businesses with further work to be carried out on scope and carve-outs. The financial services industry is identified as a sector that may be considered for a carve-out, taking into account the tax policy rationale as well as other practicalities.
- New Nexus. A new nexus rule would apply to a business with a sustained and significant involvement in the economy of a market jurisdiction, such as through consumer interaction and engagement, irrespective of physical presence. A revenue threshold in a market would be a primary indicator of a sustained and significant involvement in that jurisdiction. The proposal would create nexus for business models that sell directly to consumers or through a distributor.
- New Profit Allocation Rules. Once it is determined that a country has a right to tax profits of a non-resident enterprise, new rules would determine how much profit to allocate to the relevant jurisdiction. The Unified Approach proposes a transfer pricing system that purports to largely retain the arm’s length principle but complements it with a formulary three-tier mechanism – Amounts A, B, and C – representing different types of taxable profit.

    - Amount A – an unspecified portion of deemed residual profit. The deemed residual profit would be the profit that remains after allocating deemed routine profit on activities to the countries where the activities are performed. The eligible market jurisdictions would receive some specified share of the residual profits based on a previously agreed allocation key (e.g., sales).
    - Amount B – fixed return for baseline activity (i.e., routine marketing or distribution functions). Activities in a market jurisdiction, and in particular distribution functions, would remain taxable according to existing rules (e.g., transfer pricing under the arm's length principle and permanent establishment allocation) with the possibility of using fixed remunerations.
    - Amount C – additional profit. Taxpayers and market jurisdictions would retain the ability to argue that the marketing and distribution activities taking place in the market jurisdiction go beyond the baseline activity and therefore warrant a profit in excess of the fixed return contemplated in Amount B, or that the taxpayer performs other activities in the jurisdiction unrelated to marketing and distribution.
- Elimination of Double Taxation. It will be important to explore to what extent existing mechanisms for eliminating double taxation can continue to operate effectively. In addition, approaches to address any risk of double counting or duplication between three possible types of taxable profit would need to be considered.
- Implementation Issues. Different approaches could be developed to streamline the implementation of these changes. An important political consideration is the need for the implementation to occur simultaneously by all jurisdictions to ensure a level playing field.

The OECD has requested comments on the proposed Unified Approach no later than November 12, 2019. ICI Global will schedule a call with the Management Company Tax Subcommittee and other members interested in these issues to develop an industry response.

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endnotes

[1] See Institute Memorandum 31808, dated June 14, 2019.