Brussels, November 12, 2019

VIA ELECTRONIC TRANSMISSION: TFDE@OECD.ORG

Tax Policy and Statistics Division, Centre for Tax Policy and Administration
Organization for Economic Cooperation and Development
2 rue André Pascal, 75016 Paris, France

Re: CCIA response to the OECD consultation on Secretariat Proposal for a Unified Approach to the Nexus and Profit allocation challenges arising from Digitalisation (Pillar 1)

The Computer & Communications Industry Association (CCIA) is an international, nonprofit association representing a broad cross section of computer, communications and Internet industry firms. CCIA remains dedicated, as it has for over 40 years, to promoting innovation and preserving full, fair and open competition throughout our industry.[1]

Industry welcomes the ambition and progress made by the OECD to achieve multilateral consensus to update the international tax framework in a coherent way by end 2020. The international community is making important progress and CCIA supports the OECD's great efforts to achieve a global consensus.

CCIA agrees with the OECD's focus on changing the profit allocation rules based on operating profit. CCIA is concerned, however, that the proposal as currently drafted could still be very narrow. Contrary to the ambition of the OECD secretariat and many member states, this risks leading to a ring-fencing of highly digitised business models and certain Internet companies.

CCIA's attached comments respond to questions raised by the consultation.

Thank you for the consideration of these comments.

Sincerely,

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CCIA's Submission to the OECD Consultation on the Secretariat Proposal for a "Unified Approach" under Pillar One

[1] A full list of CCIA members is available at: www.ccianet.org/members.

Executive Summary

1. CCIA welcomes the ambition and progress made by the OECD to achieve multilateral consensus to update the international tax framework in a coherent way by end 2020. **We agree with the OECD's focus on changing the profit allocation rules based on operating profit.**
2. The solution should work for all countries (developed and developing) and be implementable in a practical way for both businesses and tax authorities. This should **reduce disputes, promote tax certainty and prevent multilayer taxation**. As CCIA outlined in comments in the Spring, the following overarching tax design principles should continue to guide discussions: multilateralism, evidence-based, business model neutrality, profit-based, should prevent double taxation and unintentional non-taxation, and simplicity and predictability.[2]
3. **CCIA warns against a too narrow scope.** CCIA supports an ambitious reform, as the entire world economy is becoming increasingly digital. CCIA would not support a solution that involves ring-fencing "consumer-facing" businesses, as this is arbitrary and too ambiguous and would likely lead to disputes. Furthermore, if the solution only applies to certain business models, this would force companies to prepare bespoke, segmented financials, which would also lead to complexity and uncertainty. To realize the OECD's ambition of "ensuring [that] all MNEs pay their fair share" **the scope of Pillar I should apply broadly**, with limited exemptions for certain sectors that are little or not subject to digital transformation.
4. The unified approach would likely set up a **new concept of enhanced nexus**, granting taxing rights to countries where companies do not necessarily have a permanent establishment, which will require changes to tax treaties and countries' domestic law. Treaty changes creating this new nexus rule should explicitly state that the rule is purely for the purposes of corporation tax / the market allocation and does not create nexus for VAT purposes (or other purposes).
5. As part of the Pillar 1 multilateral agreement, there should be an **explicit commitment from all participating countries to remove any existing unilateral Digital Services Taxes** and not to enact any further DSTs which the OECD has previously indicated undermines global solutions.

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[2] Comments of CCIA, OECD consultation on the possible solutions to the tax challenges of digitalisation, filed March 6, 2019, *available at* http://www.ccianet.org/wp-content/uploads/2019/07/CCIA-Response-To-OECD-Tax-Consultation.pdf.

I. Scope of the Pillar I unified approach

The proposed scope of the Pillar 1 unified approach falls short with respect to promoting certainty and creating a practical solution to global tax challenges. The OECD has long established that the entire global economy is digitising. However, the proposal's scope appears very narrow.

CCIA has serious concerns with the use of an ambiguous scope focused on "consumer-facing businesses."[3] Arbitrary ring-fencing is distortive and ambiguous, and will lead to disputes and tax uncertainty. It is very difficult to determine where to draw the line as to what constitutes a "consumer facing" business, and any such distinction would be arbitrary. It is impossible to define the digital economy and any concerns with the existing international tax framework result from globalization and the broader digitalization that is occurring. In contrast, it is much less ambiguous to have a clear scope capturing all businesses, with clearly defined, specific exemptions.

Furthermore, such a definition would quickly become outdated as business models rapidly evolve and develop over time. If the solution only applies to certain business models, this would force companies to prepare bespoke, segmented financials, which would also lead to complexity and uncertainty. The basis should be existing audited global financial statements.

Particular care should be taken with respect to trade secret protection and other sensitive business information. Firms within the scope of the new rules shouldn't be required to hand over overly segmented details about their strategic business decisions which would put them at a competitive disadvantage compared to competitors not in scope.

If the OECD considers it necessary to limit the scope of the long-term solution to achieve political agreement, then we consider that it should apply to all business as a matter of principle, with possible exemptions for certain sectors that are whose global outreach is limited or otherwise not subject to digital transformation. For example, CCIA has concerns regarding the inclusion of some manufactured goods, such as those created in the semiconductor industry.

II. Allocation of taxing rights to market jurisdictions

The solution should not provide a guaranteed Amount A return for market jurisdictions (irrespective of group profitability), as would inevitably result in double taxation. Only excess profits above a deemed level of normal return should be reallocated. CCIA supports a simple and more formulaic approach over a detailed technical and subjective approach that would involve valuations or judgments.

The Amount A rules need to make clear which country/ies (and which legal entity) is the surrendering country in terms of the profits now reallocated to the market countries. The Amount A profit reallocated

[3] The approach focuses on consumer-facing businesses for whom customer engagement and interaction, data collection and exploitation, and marketing and branding is significant, and can more easily be carried out from a remote location.

must be exempt in the surrender country - CCIA does not support a credit approach, as this would be unnecessarily complex and inevitably lead to double taxation.

III. New nexus Rule

As regards the profit reallocation under Pillar I, it seems likely that changes to nexus rules are required to include a concept akin to a “virtual” presence are required, which will require changes to tax treaties and countries’ domestic laws.

Treaty changes creating this new nexus rule should expressly state that the rule is purely for the purposes of corporation tax / the market allocation and does not create nexus for VAT purposes (or other purposes). No VAT implications should arise as the result of the profit reallocation rules under the new Pillar 1 method.

Countries should agree that any profits reallocated should not result in a deemed payment or a characterization of a payment that could be subject to VAT, withholding taxes or other taxes.

IV. Trade Intangibles

Trade intangibles should be excluded from the non-routine profits to be allocated under Amount A. The amount of profit allocated to the trade intangibles should take into account the level of research and development (R&D) investment required for the different industries/sectors.

As noted in the OECD Consultation Document on Addressing the Tax Challenges of the Digitalisation of the Economy, trade intangibles do not similarly possess an intrinsic functional link with market jurisdictions.

Trade intangibles, like R&D, generally arise from substantial, observable activities arising in specific locations. These activities are not subject to portability and do not present the types of challenges attempting to be addressed in this OECD work.

Furthermore, the methods for compensating the cost incurred for R&D and trade intangibles are well established and often agreed on with tax administrators. Including R&D in this calculation could discourage jurisdictions from supporting R&D and could impact economic growth as well as foreign direct investment.

V. Avoiding Double Taxation

With the establishment of a new nexus and means of calculating group profits, it is imperative that strong parameters be included to reduce the potential for double taxation.

- *Profit Allocated to a Single Tier:* The proposal creates a new three tier mechanism (Amount A, B, and C). To ensure that routine and residual profits are not double counted, it should be made clear that income can only be categorized into a single tier. For example, if income is determined that is should be calculated under Amount A, that same income cannot also be calculated under Amount B and/or C.
- *Advanced Pricing Arrangements (APAs)*: Unilateral and multilateral APAs have existed for years and permit a taxpayer and taxing authority to solve potential tax disputes in a cooperative manner.

These arrangements generally take years to establish and reduce uncertainty for all parties. APAs should continue to play a strong role and remain in force regardless of the changes made in this new system. These mechanisms are important to reducing disputes, particularly under Amount C.

- *Top-Down Allocation:* The new mechanisms should be applied on a top-down basis to avoid double taxation. Much of this current discussion relates to the activities of the parent company and their subsequent allocation to their subsidiaries. Therefore, the three proposed mechanisms should use the parent company (and its corresponding accounting standard) as the starting point for any of these calculations. The profit allocation calculations should be performed centrally at the parent company level using the parent company jurisdiction's tax and accounting principles. This would ease compliance and more accurately reflect the economic reality of the company.
- *Accounting Principles*: A consistent standard is essential to reducing disputes and avoiding double taxation. As different countries apply different accounting principles, companies need to be able to utilize a consistent basis for the starting point of calculations and use a single methodology for any appropriate tax adjustments. As part of the process, it is also imperative that any unilateral measures that countries have adopted or enacted be repealed as part of this adoption.

VI. Commitment to remove unilateral digital taxes

As part of the Pillar 1 multilateral agreement, there should be an explicit commitment from all participating countries to remove any existing unilateral Digital Services Taxes and not to enact any further DSTs. It is concerning that a number of the national digital taxes do not include a sunset provision in the legislation implementing the tax, despite statements from policymakers stating their intent to remove taxes once the OECD reaches a solution. A final agreement under Pillar 1 should include commitments to do so.