

Pillar One - Amount B

Response by the Chartered Institute of Taxation

1 Introduction

- 1.1 The Chartered Institute of Taxation (CIOT) is the leading professional body in the UK for advisers dealing with all aspects of taxation. We are a charity and our primary purpose is to promote education in taxation with a key aim of achieving a more efficient and less complex tax system for all. We draw on the experience of our 19,000 members, and extensive volunteer network, in providing our response.
- 1.2 We are taking the opportunity to respond to the public consultation on *Pillar One - Amount B* published on 17 July 2023. We recognise the significant ongoing work by the OECD/G20 Inclusive Framework on BEPS and we support the principles and the intentions around Amount B: of simplifying and streamlining the transfer pricing of baseline marketing and distribution activities in accordance with the arm's length principle. We understand that the aim is also to increase tax certainty and reduce resource-intensive disputes between taxpayers and tax administrations in respect of these transactions. The framework for Amount B, including the scoping criteria and pricing methodology, is moving towards meeting these principles, but we continue to have concerns about the potential effectiveness in meeting the aims for Amount B.
- 1.3 We welcome that the proposals in the consultation document are greatly simplified from those presented in the last public consultation at the start of the year. In particular, we welcome the work that has been done to arrive at the pricing matrix. While a business will still need operational transfer pricing expertise, this will reduce the amount of functional analysis that has to be undertaken to identify and categorise transactions and seems sensible.
- 1.4 We note that open issues remain and the proposals do not represent a consensus view of the Inclusive Framework. In taking this work forward, we would strongly encourage the Inclusive Framework to continue to simplify the proposals to the greatest extent possible in order to ensure that Amount B provides businesses and tax administrations with a tangible benefit and achieves its objectives. To be of real benefit Amount B needs to reduce the amount of transfer pricing work that must be undertaken by multinational enterprises (MNEs) and remove a significant amount of activity from transfer pricing disputes.
- 1.5 We remain concerned about the resourcing burden for tax authorities. The Pillars introduce a completely new level of complication over and above the various measures that have already been introduced or adopted in recent years because of the BEPS project. It is not practical to continue to place increased administrative

burdens on tax authorities when many are already struggling to maintain service levels because of administering their own jurisdictions' tax rules.

- 1.6 We have considered the proposal of Amount B in the light of the CIOT's objectives for the international tax system. These objectives are that a tax system should comprise rules which translate policy intentions into law accurately and effectively, without unintended consequences. The tax system should aim to provide simplicity (so far as possible) and clarity, so businesses can understand how much tax they should be paying and why, and also to provide certainty so that businesses can plan ahead with confidence. It is also important that there is responsive and competent tax administration, with a minimum of bureaucracy. In light of the relatively short consultation period we have limited our comments to high-level points around underlying principles and key concerns that have been raised with us. We are aware that many other stakeholders (including the Big 4 accounting firms and the MNEs that will be within the scope of the rules) are engaged with the OECD and the consultation process, and will be feeding in points of detail.

2 About us

- 2.1 The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. Our comments and recommendations on tax issues are made solely in order to achieve this aim; we are a non-party-political organisation.
- 2.2 The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.
- 2.3 The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries.
- 2.4 Our members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.

3 Safe harbour and implementation

- 3.1 The framework in the consultation document presents Amount B as being implemented through inclusion in the OECD Transfer Pricing Guidelines (TPG), suggesting that Amount B will be mandatory, prescribing the interpretation of how the arm's length principle applies to baseline marketing and distribution activities within its scope, rather than a safe harbour. However, a footnote indicates that further consideration will be given to the different means of implementing Amount B.
- 3.2 Businesses would find Amount B more beneficial as an elective safe harbour, rather than being mandatory for transactions within its scope. There are situations where the outcomes from mandatory application will be inappropriate as a result of the business being genuinely different from the models envisaged by the pricing matrix (for example a start-up business where the pricing matrix could result in more profit being allocated to the distributor than is in the value chain).

- 3.3 Also, mandatory application of Amount B may complicate the transfer pricing analysis for businesses where there is no clear distinction between the baseline distributor and other functions/transactions (for example, the cost base of the baseline distributor includes other transactions such as support services to the distributors). In this scenario, the MNE would be required to undertake a full transfer pricing analysis for its other transactions and functions before applying Amount B. Amount B will be dependent on the group's overall results, which depends on overall transfer pricing position. This means that the transfer pricing has to be settled first before Amount B can be properly calculated. It would be preferable if Amount B were an elective safe harbour, permitting businesses for whom it would be a complication rather than a simplification to elect not to use it.
- 3.4 We do not think that the administrative burden would be any more or less for low capacity jurisdictions if Amount B were a safe harbour, rather than mandatory. This is because these jurisdictions will have to undertake full transfer pricing for transactions that are outside of the scope of Amount B (which is narrow – see below) in any event, and will, therefore, have to build capacity for both sets of rules. We can also see an argument that if Amount B is optional, it could be seen to undermine the argument that Amount B is arriving at an arm's length price; because similar transactions opting to use full transfer pricing rather than Amount B may arrive at a different price. However, in reality Amount B must be accepted to be only an approximation of an arm's length price, and arm's length pricing operates across a range in any event.
- 3.5 We also recognise that Amount B is meant to be an advantage to low capacity jurisdictions because it would enable them to receive a certain amount of income from baseline activities without the tax authority having to conduct the amount of work that is required under the existing rules. We understand that if Amount B is not mandatory, there may be a perception that this benefit for low capacity jurisdictions may not arise. However, provided the safe harbour is fulfilling the aims of simplicity, we anticipate that it will be used by businesses. Thus, overall, we would prefer to see Amount B introduced as an elective safe harbour.
- 3.6 The framework says that the Amount B rules will be incorporated into the TPG by January 2024, but the mechanisms and processes for implementation remain unclear. We understand that further work will be undertaken in respect of implementation, including the timetable to take account of the time businesses need to prepare. This is welcome. Ordinarily changes to the TPG would take effect at different times in different jurisdictions, depending on how each jurisdiction incorporates the TPG into their regimes.

4 Scope and qualifying criteria

- 4.1 Although broadened to some extent, the scope of Amount B remains narrow. This will limit the usefulness of the measure.
- 4.2 It is envisaged that distributors that perform non-distribution transactions can still be in scope of Amount B, but an accurate delineation of the in-scope transactions will have to be undertaken. This additional flexibility is welcome, however, the segmentation of the different activities is a 'bright line' test. We suggest that consideration should be given to permitting immaterial other activities to remain within scope of Amount B in order to reduce the work that would otherwise have to be done to separate out the activities. We suggest that if the non-baseline activities do not change the transfer pricing outcomes, they should be considered to be immaterial and can be ignored.
- 4.3 We welcome the work that has been done to simplify the qualifying criteria for Amount B. With regard to 'alternative B' in the consultation document, which sets out a separate qualitative scoping criteria to exclude entities that make non-baseline contributions, in our view this is probably not required. The proposed criteria

include enough direction as to what are baseline and what are non-baseline activities without the additional scoping criteria. Additionally, including an exclusion for non-baseline activities, without an explicit definition of baseline activities, adds to the complexity of the proposals, and may be seen as confusing.

- 4.4 As drafted, the qualitative test introduces more examples into the TPG, which may make it easier to understand the tests. However, those examples could be included in any event as examples of when Amount B would and would not apply.
- 4.5 Should the qualitative test be included, consideration should be given to removing some of the other tests – for example, the Berry ratio ‘cap and collar’ test.
- 4.6 The overriding principles should be one of simplification and ensuring that the work that is required to ascertain whether Amount B applies is kept to a minimum. Scoping criteria should not be included unless it is clear that they are required to produce a different result. Overall, an additional qualitative scoping criteria would disproportionately add to the work required, and mean that most of what is required for a full transfer pricing analysis must be undertaken. Thus in our view it should not be included.

5 Other points

- 5.1 Transparency: we would welcome some transparency around the statistics and econometrics (where the data used is coming from and what has been done with it to get to the position taken). The OECD has not published its underlying economic analysis showing how the pricing matrix has been arrived at, for example. It is important that businesses are confident in the data sets being used to arrive at the matrices being used.
- 5.2 Documentation: we welcome that the documentation requirements have been made much less prescriptive. Businesses will welcome that they are aligned with the existing general guidance for local file information under the TPG.
- 5.3 Tax certainty: the proposals around tax certainty in the framework are sensible. However, whilst Amount B is intended to enhance tax-certainty and reduce the potential for disputes, there is a danger that, in practice, it will merely change the focus of disputes. Currently, tax authorities may typically challenge a business’s benchmarking analysis. Under Amount B the emphasis may be instead on the nature of the activities carried on and the extent to which they are within the scope of Amount B. This is why clarity and simplicity around the scoping criteria is critical in the ongoing work to finalise the proposals, to ensure that there is a reduction in the amount of transfer pricing disputes.

6 Acknowledgement of submission

- 6.1 We would be grateful if you could acknowledge safe receipt of this submission, and ensure that the Chartered Institute of Taxation is included in the List of Respondents when any outcome of the consultation is published.

The Chartered Institute of Taxation
31 August 2023