

To: Organization for Economic Cooperation and Development
Centre for Tax Policy and Administration
Tax Treaties, Transfer Pricing and Financial Transaction Division

Via e-mail: tfde@oecd.org

From: Foglia & Partners

Re: Comments on “Pillar One – Amount A: Draft Multilateral Convention Provisions on Digital Services Taxes and other Relevant Similar Measures”

Date: 20 January 2023

Ladies and Gentlemen,

We appreciate the opportunity to submit these comments on behalf of Foglia & Partners on the public consultation document “Pillar One – Amount A: Draft Multilateral Convention Provisions on Digital Services Taxes and other Relevant Similar Measures” (“**Consultation Document**”) released by the Organisation for Economic Cooperation and Development (“**OECD**”) on 20 December 2023 and to contribute to the ongoing global discussion of these important tax policy matters.

We recognise that the OECD Secretariat has made extended efforts in elaborating the valuable inputs provided by the stakeholders in the context of the previous public consultations and in developing the draft technical rules of Amount A. At this stage, we believe that the contribution of the stakeholders to the works on Pillar One should continue to support the fine-tuning of the different opened “building sites” of Amount A. The present Consultation Document offers the chance of perfecting those provisions, additional to the operative provisions on Amount A, regarding the withdrawal of all existing digital services taxes and relevant similar measures and the related commitment not to implement such measures in the future.

In order to facilitate the reading of our comments, please have in mind that the words with capital letter, if not specifically defined in the present document, should have the same meaning they have in the Consultation Document.

The following is the table of contents:

TABLE OF CONTENTS

| | |
|--|---|
| <i>Comments on the Consultation Document</i> | 2 |
|--|---|

| | | |
|------|---|---|
| 1. | <i>Article 37: Removal of Existing Measures</i> | 2 |
| 1.1. | <i>Scope of the obligation not to apply existing “offending” measures</i> | 2 |
| 1.2. | <i>Targets of the prohibited existing “offending” measures</i> | 6 |
| 2. | <i>Article 38: Removal of Existing Measures</i> | 7 |

Comments on the Consultation Document

1. Article 37: Removal of Existing Measures

1.1. *Scope of the obligation not to apply existing “offending” measures*

Article 37 contains provisions requiring contracting States to withdraw from applying all existing measures identified and listed in a specific list contained in a dedicated annex of the MLC to any company.

In particular, according to Article 37, paragraph 1:

“A Party shall not apply any measure listed in Annex A (List of Existing Measures Subject to Removal) to any company² as from the date on which this Convention enters into effect with respect to that Party.”.

The current wording of Article 37 provides for a prohibition to apply only in relation to the existing measures identified and listed in a specific annex to the MLC. It does not contain a general prohibition to apply digital services taxes or relevant similar measures.

As a consequence, States parties to the MLC do not have an obligation not to apply the digital services taxes or relevant similar measures other than those included in Annex A. However, pursuant to Article 38, paragraph 1, States that do have digital services taxes or relevant similar measures in force and in effect face the same consequences of those States that maintain in force and in effect the measures listed in Annex A; *i.e.*, they cannot be allocated profits under Amount A implementing provisions and they cannot impose taxes under Amount A domestic implementing provisions.

Since the consequences of the violation of the prohibition contained in Article 37, paragraph 1, are the same in relation to measures listed in Annex A and digital services taxes or relevant similar measures, we believe that the prohibition of Article 37 should be extended also vis-à-vis the digital services taxes or relevant similar measures as defined in Article 38, paragraphs 2 and 3.

This approach would have the following advantages:

- (i) it would stress the importance of a commitment by the States parties to the MLC to remove all – not only those identified and listed in the Annex A of the MLC – existing “offending” measures and not to implement new ones; and
- (ii) it would solve the problems foreseen in the footnote No. 1 of the Consultation Document regarding how to treat those measures not included in Annex A, but identified as a “digital services tax or relevant similar measure” by the Conference of the Parties pursuant to the proposed paragraph 4 of Article 38, as well as whether to include such measures in the Annex A and how to address existing measures of Parties that join the MLC after it enters into force. Indeed, a new wording of Article 37 would have the following consequences:
 - would not require the inclusion of a “digital services tax or relevant similar measure” in the Annex A to be considered prohibited under Article 37;
 - would not require a continuous update of the Annex A (in case the Conference of the Parties identifies an existing measure as a “digital services tax or relevant similar measure” pursuant to Article 38 or in case a new Party applying a “digital services tax or relevant similar measure” joins the MLC after it enters into force).

To this end, we suggest to evaluate whether to move the definition of “digital services tax or relevant similar measure” contained in Article 38, paragraphs 2 and 3, to Article 37.

As a result, we propose to amend Article 37 and Article 38 as follows:

“Article 37: Removal of Existing Measures

1. *A Party shall not apply a **digital services tax or relevant similar measure**, or any measure listed in Annex A (List of Existing Measures Subject to Removal), to any company as from the date on which this Convention enters into effect with respect to that Party.*
2. *For purposes of this Article, the term “digital services tax or relevant similar measure” shall mean any tax imposed by a Party, however described, if it meets all of the following criteria and is not described in paragraph 3:*
 - a. *the application of such tax, or the amount of tax imposed, is determined primarily by reference to the location of customers or users, or other similar market-based criteria;*
 - b. *such tax either:*
 - i. *is applicable by its terms solely to persons that:*

1. *are not residents of that Party (“non-residents”);*
or
2. *are primarily owned, directly or indirectly, by non-residents of that Party (“foreign-owned businesses”); or*
- ii. *is applicable in practice exclusively or almost exclusively to non-residents or foreign-owned businesses as a result of the application of revenue thresholds, exemptions for taxpayers subject to domestic corporate income tax in that Party, or restrictions of scope that ensure that substantially all residents (other than foreign-owned businesses) supplying comparable goods or services are exempt from its application; and*
- c. *such tax is not treated as an income tax under the domestic law of the Party, or is otherwise treated by that Party as outside the scope of any agreements (other than this Convention) that are in force between that Party and one or more other jurisdictions for the avoidance of double taxation with respect to taxes on income.*
3. *The term “digital services tax or relevant similar measure” shall not include:*
 - a. *a rule that addresses artificial structuring to avoid traditional permanent establishment or similar domestic law nexus requirements that are based on physical presence (including both direct physical presence and the physical presence and activity of an agent);*
 - b. *value added taxes, goods and services taxes, sales taxes, or other similar taxes on consumption; or*
 - c. *generally applicable taxes imposed with respect to transactions on a per-unit or per-transaction basis rather than on an ad valorem basis.*
4. *Listing or not listing a specific measure in Annex A:*
 - a. *shall not be considered evidence as to whether or not that measure is described in paragraph 2 ~~of Article 38~~; and*
 - b. *shall determine that measure’s treatment solely for purposes of this Convention.*
5. *The definition of ‘digital services tax or relevant similar measure’ in paragraph 2 shall apply solely for purposes of this Convention.”*

“Article 38: Provision Eliminating Amount A Allocations for Parties Imposing DSTs

and Relevant Similar Measures

1. Any Party for which a digital services tax or relevant similar measure, or a measure listed in Annex A (List of Existing Measures Subject to Removal), is in force and in effect during a Period:
 - a. shall not be allocated any profit under [the MLC provision allocating Amount A] with respect to that Period; and
 - b. shall not impose tax with respect to that Period under any domestic law provision implementing the provisions of [the MLC provision allocating Amount A].
- ~~2. For purposes of this Article, the term “digital services tax or relevant similar measure” shall mean any tax imposed by a Party, however described, if it meets all of the following criteria and is not described in paragraph 3:~~
 - ~~a. the application of such tax, or the amount of tax imposed, is determined primarily by reference to the location of customers or users, or other similar market-based criteria;~~
 - ~~b. such tax either:~~
 - ~~i. is applicable by its terms solely to persons that:~~
 - ~~1. are not residents of that Party (“non-residents”);~~
 - ~~or~~
 - ~~2. are primarily owned, directly or indirectly, by non-residents of that Party (“foreign-owned businesses”); or~~
 - ~~ii. is applicable in practice exclusively or almost exclusively to non-residents or foreign-owned businesses as a result of the application of revenue thresholds, exemptions for taxpayers subject to domestic corporate income tax in that Party, or restrictions of scope that ensure that substantially all residents (other than foreign-owned businesses) supplying comparable goods or services are exempt from its application; and~~
 - ~~c. such tax is not treated as an income tax under the domestic law of the Party, or is otherwise treated by that Party as outside the scope of any agreements (other than this Convention) that are in force between that Party and one or more other jurisdictions for the avoidance of double taxation with respect to taxes on income.~~
- ~~3. The term “digital services tax or relevant similar measure” shall not include:~~
 - ~~a. a rule that addresses artificial structuring to avoid~~

- ~~traditional permanent establishment or similar domestic law nexus requirements that are based on physical presence (including both direct physical presence and the physical presence and activity of an agent);~~
- ~~b. value added taxes, goods and services taxes, sales taxes, or other similar taxes on consumption; or~~
- ~~c. generally applicable taxes imposed with respect to transactions on a per-unit or per-transaction basis rather than on an ad valorem basis.~~

~~4.2.~~ A Party shall be considered to have a digital services tax or relevant similar measure in force and in effect if:

- ~~a.~~ it is determined by the Conference of the Parties to have enacted a measure described in paragraph 2 of Article 37; and
- ~~b.~~ the Conference of the Parties has not determined that the Party has withdrawn that measure or otherwise terminated its application with respect to all companies.

~~5.3. The definition of ‘digital services tax or relevant similar measure’ in paragraph 2 and Any determination under paragraph 42 shall apply solely for purposes of this Convention.”.~~

1.2. Targets of the prohibited existing “offending” measures

As already noticed, the prohibition to apply existing measures identified and listed in Annex A of the MLC is intended to prevent the application of those measures to “any company”.

In particular, according to Article 37, paragraph 1:

“A Party shall not apply any measure listed in Annex A (List of Existing Measures Subject to Removal) to any company as from the date on which this Convention enters into effect with respect to that Party.”.

In this respect, the footnote No. 2 of the Consultation Document remarks that

“Consideration will be given to whether any existing measure could continue to be applied against an MNE with a UPE located in a jurisdiction that is not Party to the MLC, and to whether the commitment discussed below with respect to future measures should permit application to such MNEs.”.

We believe that, in order to preserve the deterring effect of the prohibition contained in Article 37 to apply domestic “offending” measures, it would be preferable to maintain the prohibition as more unconditioned as possible. Therefore, States parties to the MLC

should not be allowed to apply existing “offending” measures vis-à-vis MNE with a UPE located in a jurisdiction that is not party to the MLC.

2. Article 38: Removal of Existing Measures

As a consequence of the violation of the prohibition to apply digital services taxes or relevant similar measures, or a measure listed in Annex A, Article 38, paragraph 1, provides that States parties to the Convention

“shall not be allocated any profit under [the MLC provision allocating Amount A] with respect to that Period; [...]”.

In the footnote No. 4, the Consultation Document explains, in relation to the abovementioned provision, that

“Consideration will be given to whether full denial is appropriate in all circumstances, or whether denial should be in some respect proportional to the scale of the offending measures (e.g., in terms of revenue raised). This work will also examine the situation in which a Party adopts a measure that has only de minimis impact.”.

We believe that a full denial of the profit allocation under the MLC provision allocating Amount A could be more beneficial. It should serve better the aim of the provisions that is deterring States from continuing to apply their domestic “offending” measures.

* * *

Hoping that you will find our comments useful, please do not hesitate to contact us if you require any clarification.

We welcome the opportunity to discuss these comments in greater detail and to continue to participate in the dialogue as the OECD and country policymakers advance the work on this important project.

Yours sincerely,

Foglia & Partners



To: Organization for Economic Cooperation and Development

Via e-mail: transferpricing@oecd.org

From: Foglia & Partners

Re: Comments on “Pillar One – Amount B”

Date: 25 January 2023

Ladies and Gentlemen,

We appreciate the opportunity to submit these comments on behalf of Foglia & Partners on the public consultation document “Pillar One – Amount B” (“**Consultation Document**”) released by the Organisation for Economic Cooperation and Development (“**OECD**”) on 8 December 2022 and to contribute to the ongoing global discussion of these important tax policy matters.

We recognise that the OECD Secretariat has made extended efforts in elaborating the valuable inputs provided by the stakeholders in the context of the previous public consultations and in developing the main design elements of Amount B. At this stage, we believe that the contribution of the stakeholders to the works on Amount B should focus on giving input on the technical design of Amount B, on which the Inclusive Framework (“**IF**”) has not yet reached a final view. Therefore, our comments deal with those substantial aspects we deem to be of utmost importance for the technical design of Amount B.

In order to facilitate the reading of our comments, please have in mind that the words with capital letter, if not specifically defined in the present document, should have the same meaning they have in the Consultation Document.

The following is the table of contents:

TABLE OF CONTENTS

| | |
|---|---|
| <i>Comments on the Consultation Document</i> | 2 |
| 1. <i>Scope of Amount B</i> | 2 |
| 1.1. <i>General considerations</i> | 2 |
| 1.2. <i>Role of written agreements within the in-scope analysis</i> | 3 |
| 1.3. <i>Multi-activities entities</i> | 5 |

| | | |
|----|---|---|
| 2. | <i>Documentation requirements</i> | 5 |
| 3. | <i>Tax certainty</i> | 6 |

Comments on the Consultation Document

1. Scope of Amount B

1.1. General considerations

According to the Consultation Document, verifying whether intra-group transactions are eligible for Amount B require the assessment of both qualitative criteria, connected with the economically relevant characteristics of the transactions, and quantitative criteria, which may establish permissible thresholds (*e.g.*, in case of permitted net sales generated from customers located abroad¹ or in case of the allowed ancillary activities²) or might be used to evaluate whether a distributor might own economically relevant intangible assets.

We believe that this approach departs from the contents of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (“**TP Guidelines**”), which remark, in Chapter I, Section D.1.2, the essential role of a proper and sound functional analysis, aimed at identifying the economically significant activities and responsibilities undertaken, assets used or contributed, and risks assumed by the parties to the transactions.

In particular, in a post-BEPS transfer pricing world, specific importance should be devoted to understand how value is generated by the group as a whole, the interdependencies of the functions performed by the associated enterprises with the rest of the group, and the contribution that the associated enterprises make to that value creation.³ In this respect, within the functional analysis, in case of existence of an intangible, peculiar emphasis should be placed in verifying the manner in which it contributes to the creation of value in the transactions under review, the important functions performed and specific risks assumed in connection with the development, enhancement, maintenance, protection and exploitation of the intangible and the manner in which it interacts with other intangibles, with tangible assets and with business operations to create values.⁴

We believe that the proper definition of the scope of Amount B should be essentially

¹ Consultation Document, paragraph 18, let. b).

² Consultation Document, paragraph 18, let. h).

³ See TP Guidelines, paragraph 1.51.

⁴ See TP Guidelines, paragraph 6.12.

based on a solid functional analysis, conducted according to the principles provided by the TP Guidelines. A possible practical solution could be to design the scoping criteria as a list of key elements of the functional profile of a limited risks distributor, a commissionaire, an agent or a full-fledged distributor, so that such scoping criteria could function as getaways for the enterprise to qualify as a limited risks distributor, a commissionaire, an agent or a full-fledged distributor, thus being easily categorised as an in-scope entity or not.

A similar solution would be easy to implement and would require less efforts both from the MNEs' side and the tax authorities' side, since it leverages on well-known transfer pricing concepts and could easily rely on the information that are already required by Chapter V of TP Guidelines to be provided in the transfer pricing documentation (especially in the local file).

On the contrary, we are afraid that a different approach, as the one adopted in the Consultation Document, besides being not in line – as said above – with the indications of the TP Guidelines, could lead to the adverse outcome of excluding from the scope of Amount B – only for a mere “quantitative criterion” argument – certain entities which do not have a functional profile significantly different from that of a limited risks wholesaler. For example, the Consultation Document approach would exclude from the scope of Amount B entities carrying out activities of distribution to end-users,⁵ despite the circumstance that it is likely that the functional profile of a limited risks wholesaler does not diverge substantially from that of a limited risks retailer. The same could be said in relation to an enterprise that bears significant marketing and advertising costs in a single year, but does not have any control on the marketing policy, whose function – and so the related significant risks – is fully exercised by an associated enterprise abroad.

1.2. Role of written agreements within the in-scope analysis

Paragraph 26 of the Consultation Document provides that

*“Taxpayers that assert that they are within the scope of Amount B must document their qualifying transactions in a written contract that reflects the division of responsibilities, obligations and rights and the assumption of the economically significant risks associated with the distribution activities. For the application of Amount B, these elements should be consistent with the scoping criteria outlined in section 3.1 as clarified further in section 3.3. Section 5 provides additional guidance on the recommended elements to be reflected in the written contract.”*⁶

⁵ Consultation Document, paragraph 18, let. h).

⁶ Similarly, see paragraph 18, let. a), of the Consultation Document.

In other words, the Consultation Document considers written agreements essential and mandatory in order for the taxpayers to apply Amount B.

This approach is far too strict and is not in line with that adopted in the TP Guidelines (Chapter I, Section D.1.1)⁷, which affirm that the written agreements may (not must) exist and they merely constitute a starting point in the transfer pricing analysis and, on a stand-alone basis, are unlikely to provide all the relevant necessary information. Other sources are equally valuable to assess responsibilities, obligations and rights, assumption of identified risks, and pricing arrangements: the communications between the parties, the economically relevant characteristics of the transactions, the conduct of the parties.

The wrongness of the approach adopted in the Consultation Document is also testified by the fact that it allows tax administrations, when assessing whether the scoping criteria are met, to challenge the application of Amount B, even in case there is a written contract in place, on the basis of the other economically relevant characteristics of economically significant transactions, in line with the content of Chapter I of the TP Guidelines. Adopting a different approach in evaluating the importance of written agreements vis-à-vis taxpayers and tax administrations for the purposes of applying Amount B, in violation of the indications of the TP Guidelines, is an unjustified discrimination, that should be

⁷ Chapter I, Section D.1.1 of the TP Guidelines states as follows:

“1.42. [...] The controlled transactions may have been formalised in written contracts which may reflect the intention of the parties at the time the contract was concluded in relation to aspects of the transaction covered by the contract, including in typical cases the division of responsibilities, obligations and rights, assumption of identified risks, and pricing arrangements. Where a transaction has been formalised by the associated enterprises through written contractual agreements, those agreements provide the starting point for delineating the transaction between them and how the responsibilities, risks, and anticipated outcomes arising from their interaction were intended to be divided at the time of entering into the contract. The terms of a transaction may also be found in communications between the parties other than a written contract.

1.43. However, the written contracts alone are unlikely to provide all the information necessary to perform a transfer pricing analysis, or to provide information regarding the relevant contractual terms in sufficient detail.

Further information will be required by taking into consideration evidence of the commercial or financial relations provided by the economically relevant characteristics in the other four categories (see paragraph 1.36): the functions performed by each of the parties to the transaction, taking into account assets used and risks assumed, together with the characteristics of property transferred or services provided, the economic circumstances of the parties and of the market in which the parties operate, and the business strategies pursued by the parties. Taken together, the analysis of economically relevant characteristics in all five categories provides evidence of the actual conduct of the associated enterprises. The evidence may clarify aspects of the written contractual arrangements by providing useful and consistent information. If the contract neither explicitly nor implicitly (taking into account applicable principles of contract interpretation) addresses characteristics of the transaction that are economically relevant, then any information provided by the contract should be supplemented for purposes of the transfer pricing analysis by the evidence provided by identifying those characteristics.

[...]

1.45. If the characteristics of the transaction that are economically relevant are inconsistent with the written contract between the associated enterprises, the actual transaction should generally be delineated for purposes of the transfer pricing analysis in accordance with the characteristics of the transaction reflected in the conduct of the parties.”.

eliminated.

Therefore, we believe that IF should reconsider its approach, aligning to the indications of the TP Guidelines that do not require the mandatory existence of written agreements and, even in case they have been entered into, consider them as a starting point in the functional analysis that needs to be further substantiated by economic facts.

1.3. Multi-activities entities

The Consultation document seems to consider as qualifying entities those that carry out exclusively or almost exclusively (see paragraph 18, lets. c) and h)) distribution activities.

It could be considered whether this approach could be mitigated in respect to those entities that, notwithstanding they carry out multiple activities, are able to give clear and separate indications of financial results and data of each activity performed (*e.g.*, in case they have a segmented P&L account).

2. Documentation requirements

We believe that the items of information that the Consultation Document proposes to add to the information already available in the transfer pricing documentation described in the Chapter V of the TP Guidelines – and, for the present purposes, mainly in the local file – is an additional burden for enterprises that could hardly achieve simplification of the analysis and increased certainty.

In particular, we believe that some of the specific items of information listed in paragraph 87 of the Consultation Document do not add any valuable pieces of information for an accurate functional analysis, that – as said above – should be the core for the selection of the scoping criteria. For example, the request of the annual financial account of the taxpayer/tested party for the past three/five years (paragraph 87, lets. f) and g)) goes too far, without achieving any appreciable result in terms of increased accuracy of the analysis.

Moreover, as already stated above (paragraph 1.2 of the present document), the necessity of having a written contract in order for taxpayers to claim to be within the scope of Amount B is against the indications of Chapter I of the TP Guidelines, which clearly remarks that written contracts are only a starting point for the functional analysis, unable – on a stand-alone basis – to provide complete, truthful and reliable information.

Therefore, we believe that the information already required for the proper preparation of

the local file, integrated with the information provided in the master file,⁸ would be sufficient. Minor additions, linked to the proposed identification of the scoping criteria on the basis of the most appropriate functional profile for a limited risks distributor, a commissionaire, an agent or a full-fledged distributor (see above, paragraph 1.1 of the present document), could be implemented.

3. Tax certainty

We believe that the tax certainty framework described in the Consultation Document is not sufficient to prevent or address potential disputes arising in relation to the Amount B.

The proposed instruments – notably, MAPs and APAs – remain, notwithstanding the appreciable efforts devoted to improve them and make their functioning more efficient and effective and the actual hesitant results obtained so far, burdensome, costly, time-consuming and – unfortunately – often ineffective.

We believe that the tax certainty framework should be more focus in preventing possible disputes regarding both the identification of in-scope transactions and the pricing methodology. This could be achieved by designing, as proposed above (paragraph 1.1 of the present document), a simple and easily applicable – both from MNE's and tax administrations' side – framework containing the essential features characterising the functional profile of in-scope enterprises.

An elective early certainty program, shaped in a way similar to that provided for the purposes of Amount A (see Progress Report on the Administration and Tax Certainty Aspects of Pillar One), and a streamlined APA-type process could be interesting solutions to achieve certainty, provided that it is assured that the duration of the procedures is reasonable and certain and that an effective outcome is eventually obtained.

* * *

Hoping that you will find our comments useful, please do not hesitate to contact us if you require any clarification.

We welcome the opportunity to discuss these comments in greater detail and to continue to participate in the dialogue as the OECD and country policymakers advance the work on this important project.

⁸ See Consultation Document, paragraph 88.

Yours sincerely,
Foglia & Partners

A handwritten signature in blue ink, consisting of a large loop and a horizontal stroke.