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Public Consultation on the Secretariat Proposal for a “Unified Approach” under Pillar One

Dear Sir or Madam,

Thank you for the opportunity to comment on the Secretariat Proposal for a “Unified Approach” under Pillar One (hereinafter referred to as: “Secretariat Proposal”) issued on 9 October 2019.

The German Federal Chamber of Tax Advisers (hereinafter referred to as: “Bundessteuerberaterkammer”) represents the interests of more than 97,000 certified tax advisers in Germany vis-à-vis the Bundestag, the Bundesrat, the Federal Ministries, the top echelons of the civil service, the courts and the institutions of the EU and OECD.

The objectives and competencies of Bundessteuerberaterkammer include inter alia facilitating public discussions on tax matters, analysing and giving opinions on draft tax legislation and all other legislative areas that affect the tax profession in Germany and exchanging information about tax law and professional law.

Bundessteuerberaterkammer supports every measure to prevent double taxation and a fair distribution of profits between the different countries. We endorse the goal of the Secretariat Proposal to build its solution on long-standing and well-founded underlying principles of international taxation. Please find our detailed comments on the Secretariat Proposal in the enclosed document.

We would be pleased to discuss any questions you have on our comments and would welcome the opportunity to contribute to the discussion as part of the public consultation meeting 21-22 November 2019.

Yours sincerely,

i. V. Claudia Kalina-Kerschbaum
Geschäftsführerin

i. A. Steffi Balzerkiewicz
Referatsleiterin

Encl.



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Enclosure

**Public Consultation Document:
Secretariat Proposal for a “Unified Approach”
under Pillar One**

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I. General Remarks

Bundessteuerberaterkammer represents more than 97.000 certified tax advisers (*Steuerberater*) being organised as self-employed professionals or combined in partnerships or corporate entities. Same as lawyers and auditors *Steuerberater* constitute a legal profession subject to a regulatory regime especially designed for them and enacted by the parliament. *Steuerberater* form an intermediary between the state and the taxpayer. Their role is to assist the taxpayer to perform its tax obligations in compliance with the applicable law, give tax advice in accordance with tax law and defend the taxpayer rights against unjustified tax claims of the state. In this role, Bundessteuerberaterkammer is usually taking a neutral stance on questions of the economic impact of proposed new tax regimes but comments on the feasibility, consistency and adequacy of changes in law in the context of the existing tax legal system.

Our members represent German and (as far as their German tax affairs are concerned) foreign MNEs as well as SMEs in the area of tax. For all taxpayers and their advisers a tax regime which is clear, fair and easy to follow is critical. This is more than true in the field of cross border taxation as it is the subject matter of the OECD proposal laid out in the public consultation document on the Secretariat Proposal for a “Unified Approach” under Pillar One (“Secretariat Proposal”).

II. General view on the proposal

Bundessteuerberaterkammer welcomes that the OECD is addressing the challenges of taxation in a digitalised business world, seeking to achieve progress towards a global consensus-based solution.

Bundessteuerberaterkammer recognises that the current tax regimes of international enterprises are insufficient to allow remotely offered services in particular to be taxed in way granting all states a fair share. We support the development of international consensus on how to make the international tax system fit for the future.

We acknowledge that there is a certain political will to assign more taxing rights to market countries in the changing economy. In order to avoid (more) unilateral measures to tax digital activities which could lead to a patchwork of national responses we support the OECD’s endeavours to find an international consensus in this matter.

We welcome that the Secretariat Proposal focuses on highly digital business models but is not limited to them. We acknowledge that many businesses carry elements of both the digital as well as the traditional industry and therefore, a ringfencing of the digital businesses is not adequate.

Finally, we would also like to point out that taxpayers and their advisers have been confronted with a massive amount of change in relation to rules relevant for international taxation as a consequence of the OECD BEPS project: In this context, reporting obligations of businesses

have been significantly expanded despite the fact that businesses had to comply with quite comprehensive reporting obligations even before the BEPS project was initiated. Further, dispute resolution processes do not yet show material signs of improvement in practice that would ensure efficient coverage of the disputes arising from increased complexity and uncertainty. Therefore, we advocate to act with caution.

Further, in our view it is paramount that the new system provides for clear rules administrable for the taxpayers, their advisers, the tax administration and judicial bodies. Clear rules will assist tax authorities and taxpayers as well as their advisors facing these challenges. However, it is critical that any guidance given by the OECD is workable and tax authorities in all countries and taxpayers take a consistent approach.

III. Scope

1. Revenue threshold

Bundessteuerberaterkammer strongly supports the Secretariat Proposal that the new rules should have a threshold so they only apply to large businesses with a sufficient level of revenue. This is based on the notion that tax challenges raised in this context mainly relate to the fact that (large) businesses and service providers can reach markets in jurisdictions where they have little or no physical presence. These businesses can generate significant revenues in the source state with paying no or little tax. Therefore, we believe that revenues should be the reference point for the application of the new rules.

We suggest considering a threshold of 3 billion USD consolidated annual global revenue. This way it could be ensured that primarily businesses which drive the current discussion would be captured.

In any case we advocate the threshold should not be less than 750 million USD consolidated annual global revenue. Businesses with consolidated annual global revenue of 750 million USD are already subject to additional administrative rules. They would have the size, and therefore the capacity, to adopt the new rules and the additional administrative burden. We believe that a complex system that burdens small and medium-sized businesses and their advisors is not in the best interests of the global economy.

The governing principle to determine an MNE group could follow the rules for determining which companies are subject to country-by-country-reporting as both sets of rules pursue the same overarching objective, that is fighting base erosion and profit shifting, and introducing a fair taxation. Further, an existing framework could be utilised and provide consistency in the application of international tax law.

Businesses which do not meet the threshold would continue to apply the established rules. However, in order to maintain tax neutrality businesses that do not meet the threshold could be given the right to opt-in to applying the new rules. In order to promote consistency and

avoid “cherry picking” companies that choose to apply the new nexus rules could be bound on this decision for a certain time, e.g. for 3 or 5 years.

Further, the application of the new rules to a limited amount of businesses would allow taxpayers, their advisors and tax administrations to observe the application of the rules for a set period and, if necessary, adjust them. After a transition period it could be lowered to include a greater number of businesses.

2. Carve outs

Bundessteuerberaterkammer generally supports the idea of introducing carve outs for certain industries. From our point of view, extractive industries and commodities are perfect examples for stationary businesses which have never been in scope of the current discussion. We also think there are good reasons to exclude banks from the application as they are a highly regulated industry all over the world and can not do business without a physical presence in the market state.

We believe that no further carve outs other than the ones mentioned above, will be required, if a sufficient revenue threshold is introduced. The introduction of a size-based exclusion already limits the scope of application such that further limitations do not seem to be necessary.

However, if the International Framework takes further carve outs into consideration they would have to be defined very clearly. Questions raised in the consultation document show that defining the scope with reference to certain business models proves very difficult. The OECD acknowledged in previous discussions that it is not possible to “ring-fence” the digital economy. We believe that this continues to be true. Further, we expect yet unknown business models to evolve. Therefore, we suggest considering, if any, a negative definition.

IV. A new nexus rule for the taxpayers in the scope

Bundessteuerberaterkammer supports introducing the new nexus rule as a stand-alone treaty provision. This way unintended interaction between the existing rules and the new rules are in our view less likely to occur.

We also support the proposal to define the new nexus solely with reference to a revenue threshold for sales in the territory. Including other factors like users, customers, digital presence etc. would lead to complicated application rules which are likely cause disputes.

A nexus solely based on revenue can easily be identified therefore be easily administered by taxpayers, their tax advisers and tax administrations. Further, rather than introducing individual country-based thresholds for every single country we advocate for a limited number of thresholds which could take into consideration different needs of countries. Countries could be classified by certain categories. This again would contribute to the idea that the new rules should be simple and easily administrable. In any case, we believe that the threshold should

not be determined based on a country's GDP for a particular year as this would create more red tape.

The Secretariat Proposal intends to introduce the idea of including transactions with unrelated distributors in the determination of the country-based threshold (or Amount A, see below). Bundessteuerberaterkammer strongly objects against this approach. The MNE will by no means have a chance to get precise knowledge or control over the location of sale and will usually not be able to achieve financial information from unrelated parties.

V. Dispute resolution

We understand that the International Framework intends to design the new rules to be simple and provide tax certainty. However, it is nevertheless inevitable that situations will occur which may give rise to disputes. For these cases it is important that a robust dispute resolution mechanism provides an efficient and fair outcome in double tax cases.

Yet, we observe in practice that currently dispute resolution processes often do not ensure efficient coverage of the disputes arising from increased complexity and uncertainty of recently introduced BEPS measures.

In this context we would to address the two most crucial points that continue to occur in existing dispute resolution procedures and which should be addressed. First, tax disputes tend to take very long to finalise. This leaves taxpayers and their advisers in uncertainty over long periods. Second, substantial cost, especially relative to the amounts of tax in dispute, may deter taxpayers and their advisers from resolving disputes.

Therefore, Bundessteuerberaterkammer suggests to consider introducing a simplified dispute resolution for smaller amounts in dispute to provide efficient access to dispute resolution to all taxpayers. A conceivable solution could be to introduce a set of rules where the country of residence of the principal company could be obliged to provide tax relief if a certain threshold of the amount of tax in dispute is not met. A simplified procedure would enable taxpayers, their tax advisers and tax administrations to concentrate in formal procedures on resolving issues which are significant. The level of threshold would have to be discussed by the International Framework.

VI. Profit allocation

1. General Remarks

Bundessteuerberaterkammer understands that the calculation of group profits shall be based on the accounting records and accounting profits. On the positive, this information is readily available and thus reduces efforts in the first place. However, it needs to be considered that these accounting records were produced for different than taxation purposes in the first place.

In order to align the approach between countries it does seem to be consistent using the accounting method that is applied by the ultimate parent company of the group of companies. It remains unclear whether Amount A is to be seen as an additional tax, thus potentially creating an additional burden for taxpayers. This additional tax probably combines elements of different kinds of taxes (sales tax by using sales as an allocation key, destination-based tax, income tax). Actually, it needs to be ensured that any kind of “new” tax under Amount A can be relieved under the existing rules. In addition, any interference between Amount A and Amount B and C respectively has to be eliminated. Finally, a bilateral consideration for relief should be ensured in double tax treaties – either through bilateral negotiation or through an envisaged MLI process.

2. Determination of Amount A

Amount A is according to the Secretariat Proposal applicable to consumer facing businesses. We want to highlight that it remains unclear what “consumer facing businesses” or a “user” means under the unified approach. It needs to be pointed out that all goods or services will directly or indirectly be sold or transferred to a consumer or user. In addition, certain B2B transactions (which are not defined in the unified approach) could fall under the scope of Amount A. We, therefore, recommend providing clear definitions in this respect. We would welcome refinements based upon industry approaches and regional approaches.

As pointed out before, transactions with unrelated distributors can in our view not be subject to determination of Amount A under the unified approach. The scope of the unified approach should ultimately end at the moment the product or service is sold to the last point in the chain between related entities. Sales performed by intermediaries (distributors, commissionaires or sales agents) not related to the MNE group should not be considered.

We understand the approach of the Secretariat Proposal for determining Amount A as the four- step process:

1. determination of the total profit to be used, either at group level or business line level;
2. exclusion of any deemed routine profits to calculate a deemed residual by means of fixed percentages;
3. allocation of a portion of the deemed residual profit on the basis of formula to consumer facing / user activities;
4. allocation of residual profits as determined under step 3 above among the different market jurisdictions on the basis of an agreed allocation key (formulary allocation).

There is a clear risk that the formulary allocation approach under Amount A will create an excessive burden with prohibitively high costs. Therefore, it is in our view necessary that the OECD/Inclusive Framework agrees on a uniform calculation and formulary allocation approach which need to be transferred into national law. It should be considered that this is done on the basis of consolidated income determined in accordance with the accounting rules of consolidated financial statements. It is to be considered that this may subsequently lead to differences between the actual result achieved in a market state by means of consumer facing/user activities and the determination under a formulary allocation approach.

For the time being and with the information provided in the secretariat's proposal, it remains unclear how the formulary allocation approach under Amount A will be defined, as the different parameters are not yet available. Definitively, the parameters and thresholds should be set in a way so that unduly administrative burdens could be avoided, and that the economic reality could be reflected to the extent possible.

Eventually, it seems to be appropriate not to make use of Amount A as a basis for adjusting customs or any other indirect taxes.

3. Double taxation in relation to Amount A

It has been pointed out above already, that Amount A should grant access to automatic relief by providing a deduction from taxable income or exemption in the transferring jurisdiction for Amount A allocated to other jurisdictions and therefore taxation under the new nexus are to be covered under the treaties. That requires an insertion of amount A in the respective treaty.

Given the importance and the relevance of the envisaged change instruments such as including mandatory arbitration, should remain available and readily accessible to the taxpayer. As the approach is a formulary allocation approach the cases should be solved within a limited (and possibly mandatory) time frame (6 months to one year).

Further important issues to be covered are, inter alia, relief in the case of loss-making or low profit generating groups, whether these groups should not be carved out and issues related to limiting the credit of Amount A tax to the corporate income tax paid in the residence state. It should be ensured that credit of Amount A tax should be allowed to the greatest extent possible.

4. Amount B

Amount B relates to routine or baseline marketing and distribution activities. It does not seem reliable to provide a thorough definition of the functions and risks that qualify as routine or baseline marketing and distribution activities.

Therefore, Bundessteuerberaterkammer is of the opinion that these kind of routine marketing and distribution activities are functions that can be determined reliably according to normal transfer pricing rules, i.e. through benchmarking studies. For the ease of simplification, it would in our view be appropriate applying a 'safe harbour' for routine or baseline marketing and distribution activities. However, it is of importance that such a safe harbour approach is accepted by all members of the Inclusive Framework, preferably globally. Otherwise disputes would not be avoidable.

For the avoidance of doubt, it should be highlighted that any activities beyond routine or baseline activities actually are to be treated under "normal" transfer pricing rules, including activities like manufacturing, research and development, etc, would fall under application of the arm's length principle and the associated transfer pricing rules. For these activities no fixed margins in the sense of safe harbours are not applicable.

5. Amount C

It remains unclear which activities would fall under Amount C. The Secretariat Proposal deals with marketing/distribution activities in the market jurisdiction that are different (go beyond) to the routine functions (*baseline level of functionality*) and other business activities in the jurisdiction unrelated to marketing and distribution. It is not clear how 'marketing/distribution' and the meaning of the 'baseline level of functionality' is defined. A clear distinction between routine activities (Amount B) and those functionalities under Amount C is needed. Otherwise there is an increased risk that tax authorities will qualify rights under Amount C in relation to MNEs. That would in turn mean that simplification approaches as set forth under Amount B will be decreased or even be declined.