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INSIGHT: Highlights of the OECD/Inclusive Framework's Jan. 31 Statement on Pillars One and Two

BY JEFFERSON VANDERWOLK

On Jan. 31, 2020, the Organization for Economic Co-operation and Development (OECD) issued a statement on behalf of the Inclusive Framework on Base Erosion and Profit Shifting (IF) regarding the status of the IF's work on the tax challenges of digitalization. The statement reflected decisions made during a two-day meeting of the IF on Jan. 29-30. The headline news was that the IF agreed to continue its negotiations on the basis of the OECD's proposed unified approach to Pillar One (dealing with tax nexus and global profit allocation).

The statement is a 30-page document consisting of a short initial section; a lengthy segment on Pillar One issues which has two annexes (Annex A being a revised Program of Work on Pillar One, and Annex B being a decision-tree regarding the operation of the proposed Pillar One rules); and a short concluding status report regarding work on Pillar Two (the proposed global minimum tax regime).

Timing goalposts have been moved: The statement makes clear that the IF countries have not yet committed to anything beyond using the proposed unified approach (with Amounts A, B, and C) as a ''basis for negotiations'' on a without-prejudice basis. The first paragraph of the statement says that the IF countries ''affirm their commitment to reach an agreement on a consensus-based solution by the end of 2020.'' This represents a significant slippage of time in comparison to the timeline announced a year ago, when it was contemplated that agreement on the design of the solution would be reached by January 2020, leaving technical details to be worked out and reflected in a report to be delivered to the G20 by the end of 2020.

Further, the statement says that the IF is aiming to agree at its plenary meeting in early July 2020 on ''key policy features of the solution which would form the basis for a political agreement.'' Assuming this is achieved in early July, it will represent only the starting point for the detailed work needed to flesh out the solution (or solutions). The timeframe for working party meetings in the revised Program of Work on Pillar One, regarding 11 different work streams, shows that the meetings will go on until November 2020 at least. Readers should expect the work to go on throughout 2021 and perhaps beyond.

The US's safe-harbor proposal will be considered: In December 2019 the US Treasury Secretary proposed that the Pillar One regime should function as a safe harbor rather than being mandatory for all taxpayers within the scope of the rules. At a conference just two weeks before the issuance of the statement, the OECD's tax policy director, Pascal Saint-Amans, said that the safe-harbor proposal ''would not fly.'' However, the IF has decided to consider it, and will make a final decision on it after the Pillar One proposals have been developed further.

The statement says that ''many IF members'' have concerns about the US proposal, which implies that not all of the IF members are opposed to it. The statement briefly discusses the issues to be considered in connection with what is now called the ''alternative global safe harbor system.'' Some (including this author) believe there is a good chance that the safe-harbor proposal will ultimately be adopted, at least with respect to the rules regarding Amount A (formulaic allocation of residual profits to market jurisdictions).

Relevant unilateral actions would have to be withdrawn: The statement explicitly says that a commitment to the consensus-based solution on Pillar One would mean a commitment to withdraw ''relevant unilateral measures.'' The scope of relevance in this regard

will have to be defined more clearly at some point in the future: does it mean only digital services taxes? Or would special measures such as the UK's diverted profits tax also have to go?

The scope of the Amount A rules has been clarified somewhat: The revised program of work on Pillar One says two categories of businesses are in scope: automated digital services (which appears to mean internet-based businesses) and consumer-facing businesses. Regarding the latter, some helpful explanatory comments are included in the document, but some questions remain. The document explicitly excludes professional services, extractive industries ''and other producers and sellers of raw materials and commodities,'' and financial services (except possibly for any financial services that are internet-based and unregulated). Note that these scope rules are for the Amount A allocation rules only.

Some new dispute resolution processes are being discussed, but much more needs to be done: The statement has several paragraphs on possible new approaches to tax dispute resolution, but it is clear that nothing has been decided yet in this regard.

Pillar Two design work is ongoing, but the open issues have not yet been resolved: The final section of the statement is simply a brief discussion of the many open issues arising from the global minimum tax proposal. Interestingly, nowhere in the 30-page document is there an assertion of the proposition that Pillar One and Pillar Two have to be adopted together as a package in any final consensus-based solution.

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