

To: Taxation Working Group
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Subject: OECD announces workplan to change international rules for taxing MNEs

Summary

On 31 May, the OECD released a "[Programme of Work to Develop a Consensus Solution to the Tax Challenges Arising from the Digitalisation of the Economy](#)". Under the Workplan, an outline of the architecture of a long-term solution to address the challenges of the digitalisation of the economy is to be submitted to the Inclusive Framework for agreement in **January 2020**. Work will continue to flesh out the policy and technical details of the solution throughout 2020 to deliver consensus agreement on new international tax rules **by the end of 2020**. The Workplan acknowledges that this is an extremely ambitious timeline due to what it describes as "the need to revisit fundamental aspects of the international tax system." The Workplan states that this reflects the "political imperative" that the participating jurisdictions attach to timely resolution of the issues at stake.

Just like the Policy Note published earlier this year, the OECD Workplan is structured in two pillars:

- **Pillar I:** focuses on the allocation of taxing rights and seeks to undertake a review of the profit allocation and nexus rules aiming to assign additional taxing rights to market jurisdictions.
- **Pillar II:** focuses on what is described as the remaining BEPS issues and seeks to develop a global anti-base erosion proposal consisting of rules that would provide a jurisdiction with a right to "tax back" where other jurisdictions have not exercised their primary taxing rights, or the payment is otherwise subject to low levels of effective taxation.

The proposals addressed in the Workplan will have implications well beyond digital businesses or digital business models. These proposals could lead to significant changes to the overall international tax rules under which multinational businesses currently operate.

The Workplan is organised into five chapters:

- **Chapter I: Introduction** - provides detailed background on the OECD's work in this area to date.
- **Chapter II: Revised Nexus and Profit Allocation Rules (Pillar I)**
 - Makes three alternative proposals: the "user participation" proposal, the "marketing intangibles" proposal and the "significant economic presence" proposal. The aim of these proposals is to amend the existing global international rules to recognize and tax the value created by a business's activities or participation in user/market jurisdictions. While there is no consensus view yet, the Workplan notes that these options will have to be narrowed down by January 2020 to facilitate a political agreement.
 - Sets out three different methods to quantify the amount of profit to be reallocated to market jurisdictions: the modified residual profit split method, the fractional apportionment method and the distribution-based approach. The application of all three of these methods would lead to a deviation from the arm's-length principle to some extent.
 - Does not provide much information on the configuration of a new nexus rule. While the concept of remote taxable presence (i.e. a taxable presence without traditional physical

presence) is endorsed by the jurisdictions in the Inclusive Framework, a new set of standards for identifying when such a remote taxable presence exists still needs to be developed.

- Sets out a method to determine how profit should be allocated among the market jurisdictions entitled to tax under the new taxing right: The new market jurisdiction taxing right may reallocate taxing rights with respect to a proportionate part of a group's overall profit, rather than with respect to the profits from specific transactions or activities undertaken by particular separate entities.
- **Chapter III – Global anti-base erosion proposal - GloBE (Pillar Two)** sets out two inter-related rules that would apply to all types of businesses:
 - **An income inclusion rule** that would tax the income of a foreign branch or a controlled entity if that income is subject to tax at an effective rate that is below a minimum rate (and will supplement existing CFC rules).
 - **A tax on base eroding payments** that would operate by way of the denial of a deduction or imposition of source-based taxation (including withholding tax), together with any necessary changes to double tax treaties, for certain payments unless that payment is subject to tax at or above a minimum rate.
 - The Workplan provides that further work will be required on rule coordination, simplification measures, thresholds and carve-outs to ensure the GloBE proposal avoids the risk of double taxation, minimizes compliance and administration costs and has rules that are targeted and proportionate.
- **Chapter IV – Economic analysis and impact:** the Workplan provides that an economic analysis and impact assessment will be carried out. This will involve an in-depth consideration of how the proposals are expected to affect the incentives faced by taxpayers and governments, their impact on the levels and distribution of tax revenues and their overall economic effects, including their effects on investment, innovation and growth. The impact assessment also will consider how these effects vary across different kinds of multinational enterprises, sectors and economies.
- **Chapter V: Organisation of the work to deliver the Program of Work and next steps:** Following agreement on the architecture of the solution, work will continue on the policy and technical details throughout 2020 in order to deliver the consensus-based solution by the end of 2020. The Workplan indicates that public consultations may be held to obtain stakeholder feedback as the various proposals are refined but does not make a firm commitment to holding any consultations during this phase of the work.

Next steps

- As agreed at the Taxation WG meeting of 14 May, the Insurance Europe secretariat will shortly launch an internal consultation in view of finalising a "principles paper" that would be the basis of future discussions with the OECD (including a potential meeting) related to this very important work. The paper should be finalised by mid-July.