United States Council for International Business

Written Testimony of Rick Minor

The House Committee on Ways and Means

Subcommittee on Tax

Hearing on

Ensuring the Biden Administration Puts Americans First

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Chairman Kelly, Ranking Member Thompson, and members of the Subcommittee on Tax. Thank you for the opportunity to testify at this hearing on the components of the Organisation for Economic Co-operation and Development/Inclusive Framework (OECD/IF) Pillar One project (Pillar One). I am the Senior Vice President and International Tax Counsel for the U.S. Council for International Business (USCIB).

USCIB is a multi-disciplinary policy association founded in 1945, with offices in New York and Washington, DC. Our member base includes over 100 of some of the largest multinational companies from every sector of the U.S. economy and professional advisory firms. The USCIB tax committee currently consists of over 500 tax experts from our member companies and firms.

Significantly, USCIB is the U.S. affiliate to Business at the OECD (BIAC), the business advisory group to the OECD, which includes a multinational tax committee on which I and other USCIB members serve. BIAC allows USCIB an additional formal platform to represent our companies' views before the OECD and to engage directly with our tax counterparts at the business association affiliates from other OECD member states.

USCIB is also the U.S. affiliate of the International Chamber of Commerce (ICC). The ICC is the only business organization which has observer status at the United Nations General Assembly.

We are a consensus-based organization, and this is reflected in our formal consultation letters and in my comments today.

We recognize the importance of the multilateral work performed at the OECD and strive to improve the outcomes of that work by sharing the perspective of U.S. business. Given our role as the voice of U.S. business at BIAC and before the OECD, USCIB has submitted its own comment letter to every OECD Pillar One design consultation request in the last three years. On December 5, 2023, we also filed our consultation letter in response to the U.S. Treasury request for public input on the draft Pillar One Multilateral Convention ("MLC"). The MLC provides the legal framework and detailed rules for the implementation of the so-called Amount A and the removal of Digital Services Taxes (DSTs) and relevant similar measures. This statement relates to our positions in that letter and intervening developments, including the release of the February 19,

2024, version of the so-called Amount B, a simplified set of rules for pricing for tax purposes certain cross-border distribution activities.

Pillar One Observations and Recommendations

Throughout the consultation process, USCIB has emphasized its concern that the formula-based design of Amount A, as well as deficiencies with the revenue sourcing methodology and the Marketing and Distribution Safe Harbor ("MDSH"), will lead to unexpected results.

USCIB has also made the following principal recommendations:

1. **Reduce double taxation**. A solution that does not effectively eliminate double taxation is not sustainable over the long run and therefore should be a key priority for governments and the U.S. business community.
2. **Revise the definition of DSTs and other relevant and similar measures in the current draft of the MLC**. The prevention and rollback of DSTs and similar measures must be comprehensive or the MLC will have failed to stabilize the international tax system.
3. **Expand the scope of Amount B.** The scope of Amount B needs to be expanded and progress could be achieved now with the creation of a robust and explicit roadmap of future design features, including the extension of Amount B to retail sales as well as sales of digital goods and services.
4. **Stay with the multilateral process**. We encourage the Biden administration and U.S. Congress to remain engaged in the OECD process to ensure a comprehensive and durable solution to these complex international challenges now and going forward.

Amount A Background

Following the OECD's Base Erosion and Profit-Shifting (BEPS) work, many countries argued that the so-called digitalization of the economy was not properly allocating taxes among countries because companies could have significant economic activities in a country with little traditional investment in that country. This was referred to as 'scale without mass.' Scale refers to the consumer base in the country and mass to a taxable presence in that country under the traditional norms of international taxation.

These traditional norms are embedded in our tax treaty network and national laws. They require a company to establish a physical presence in a country to be subject to its taxation. The existing norms generally source profits to the location of where services are performed or where property is held (the 'source' jurisdiction), rather than where a service might be received or consumed (the 'market' jurisdiction). European countries moved unilaterally to tax companies considered to be commercially accessing their 'market' without making changes to the overall framework of the rules. These DSTs fell outside of the scope of tax treaty agreements. According to U.S. Trade Representative (USTR), these taxes were discriminatorily targeted against U.S. companies. Such taxes were also imposed on a gross basis and were not creditable against the tax base these countries were seeking to expand under Pillar One. Pillar One is the attempt to upgrade the international tax system to reallocate taxation rights to 'market' jurisdictions and eliminate the discriminatory and harmful network of DSTs and other similar measures that currently threaten to proliferate globally.

The Amount A solution applies to Multinational Enterprises (MNEs and Covered Groups) with global revenue greater than EUR 20 billion and a pre-tax profit margin greater than 10 percent of total revenue. Technically, Amount A is a formulary apportionment type of taxation and seems simple enough at a high level, but the devil is in the detail. Let me just refer here to the basics.

Amount A reallocates 25 percent of the in-scope MNE profit in excess of a 10 percent profit threshold to so-called market jurisdictions. Market jurisdictions are defined as the jurisdiction where the end-user generating the MNE revenues is located. An end-user could be where a consumer buys products or where the user of a platform accesses the internet to buy a service. The Amount A allocation number is adjusted under the so-called MDSH, if it is determined that the market jurisdiction has already taxed a portion of the profit that is in scope of Amount A. The Amount A calculation identifies the jurisdiction(s) that must relieve double taxation, which jurisdiction might or might not include a business connection to the market jurisdiction. Amount A is a novel regime that applies on top of the U.S. international tax rules for approximately 50 in-scope U.S. multinationals. The revenue threshold for the Amount A scope will be reduced to EUR 10 billion in seven years from the MLC's effective date, if the MLC were to advance in the U.S., subject to a prior multilateral review of its effectiveness.

Amount A was originally proposed to apply to consumer-facing businesses and automated digital services for MNEs that had annual revenue over EUR 750 million. As a result of the inherent difficulties in attempting to 'ring-fence' certain portions of the economy and at the behest of the Trump and then Biden Administrations, the scope of Amount A was altered to define highly profitable MNEs with revenue above EUR 20 billion. Informal analyses indicate that about 100 MNEs across a variety of industries globally would be in scope of the Amount A rules if it were in effect today.

To simplify, there is a five-step approach to determining and managing an MNE's Amount A liability.

Step one: Determine if the MNE is in scope.

Step two: Identify eligible market jurisdictions.

Step three: Calculate and allocate by a revenue-based formula a portion of the MNE excess profit.

Step four: Eliminate double taxation.

Step five: File, pay, and have access to certainty (for Amount A *and* related issues).

Observations on Detailed Components of the Multilateral Convention

Achieving these steps requires the application of a number of new technical methods and policies, which we have commented on in more detail per our public consultation letters. We would like to share some highlights from our prior letters here.

Autonomous Domestic Business Exemption

USCIB welcomes the inclusion of the autonomous domestic business exemption ("ADBE") concept in the computation of Amount A. There is work to be done on refining the rules of its application, however. In many instances the ADBE will ensure that grossly distorted outcomes will not result

from the application of Amount A, e.g., when a sizable autonomous domestic business experiences profit margins that vary significantly from the overall group. The ADBE is intended to exclude the profits of an autonomous domestic business from being inappropriately included in the Amount A base for the global profit reallocation. In the case of a U.S. group with mature, high-margin domestic stand-alone businesses, the domestic business exception will ensure that the U.S. tax base is not inappropriately subjected to reallocation under Amount A.

Marketing and Distribution Profits Safe Harbor

The OECD described the premise of the MDSH as follows. Amount A should be allocated to a market jurisdiction that is not taxing residual (or non-routine) profits under the existing profit allocation rules in place today. Amount A should not be allocated to a market jurisdiction where an MNE group already leaves sufficient residual profit that is taxed in the market. Conceptually, the MDSH would adjust the quantum of Amount A allocable to a market jurisdiction where the residual profit of the MNE group is already taxed in that jurisdiction as a result of the application of the existing profit allocation rules.[1]

USCIB members remain concerned that the MDSH does not adequately deliver on the objective to avoid double taxation. This is based on USCIB member initial modeling of the impact of the MDSH rules in the current version of the MLC. This means that the current design of the MDSH will frequently not cap the allocation of Amount A to market jurisdictions that already have taxing rights over the residual profits of a Covered Group. USCIB members are particularly concerned by the following design features that limit the effectiveness of the MDSH:

1. *De minimis* threshold of EUR 50m in profits (i.e., market jurisdictions below EUR 50m of profit are not included in the MDSH and receive a full Amount A allocation);
2. Determination of routine profit under a formulaic approach;
3. Proposed jurisdictional offset percentages that are the result of political negotiation;
4. Formulaic reductions to the Withholding Tax Upward Adjustments that may not fully relieve double taxation; and
5. Risk that these design features are amended in the future, especially if market jurisdictions are not satisfied with the Amount A outcome under the current formula.

MDSH and Withholding Taxes

The treatment of withholding taxes is of particular concern to our members. MNE modeling exercises reveal that withholding tax adjustments may be the primary determinant for whether the MDSH is effective in avoiding double counting of taxable profits in market jurisdictions. We understand the countries objecting to the withholding tax offset features within the MLC are some

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[1] OECD (2020), Tax Challenges Arising from Digitalisation – Report on Pillar One Blueprint: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris. Page 124, paragraph 501.

of the primary countries for which this calculation holds true. The reliability of the MDSH as a guardrail against double taxation will be diluted if an effective withholding tax adjustment is not provided in the final MLC text.

It is a positive step that the MLC (through the MDSH) recognizes that market jurisdictions can and do use withholding tax to tax Covered Group's residual profits, and that withholding taxes should therefore be accounted for in the MDSH. The Withholding Tax Upward Adjustment is subject to three separate limitations, a reduction factor varying between 15 percent and 70 percent, an exclusion for normal (or routine) profit, and the jurisdictional offset percentage. The effect of this means that the amount of profit accounted for when computing the MDSH will typically be 20 percent to 50 percent of the Withholding Tax Upward Amount (i.e., the profit that would need to be booked in a jurisdiction to give it equivalent taxing rights to the amount of withholding tax imposed).

USCIB members consider that there should be no reduction to the Withholding Tax Upward amount, in other words, that 100% of the relevant withholding tax imposed should be included in the MDSH calculation. The modeling indicates that the withholding tax adjustments are critically important in policing jurisdictions from double counting both Amount A and other source-based taxation methods on non-routine profits.

Moreover, where withholding taxes are not fully creditable or otherwise offset against amounts reallocated under Amount A, countries will have an incentive to override the Pillar One agreement through increases to withholding tax rates and a broadening of the scope of withholding taxes, such as through the assertion of the existence of embedded royalties.

Revenue Sourcing

We welcome the simplification of the MLC sourcing rules in response to the business community's input on the earlier OECD design drafts. However, we believe the current rules remain excessively burdensome and will lead to considerable implementation challenges. These rules can be further simplified and made more practical. We are concerned that the sourcing rules for many business-to-business revenues will nearly always result in the default selection of an OECD designed allocation key or in the use of a novel (or bespoke) sourcing methodology that will have to be agreed upon with the MNE. This will either result in a distorted allocation of profits (in the case of an allocation key) or in a significant incremental compliance burden (in the case of a bespoke method). Expanding the lists of permissible indicators to include commonly available information, such as billing addresses, would more effectively address these issues.

Additionally, we appreciate that companies should be able to rely on commercial and other available information rather than the need for new reporting obligations with the same or similar information.

Elimination of Double Taxation

Since its outset, the objective of Amount A has been to reallocate taxing rights to market jurisdictions, with a corresponding reduction in the taxing rights of residence jurisdictions. USCIB members are concerned that, as drafted, the MLC's mechanism to eliminate double taxation will result in the profits of Covered Groups being subject to double taxation in some instances. The

MLC currently relies on each adopting country to utilize their domestic laws to relieve double taxation. As a result, it is not clear to USCIB members that full double tax relief will be available due to the inevitable inconsistencies across implementing jurisdictions globally.

USCIB members encourage the U.S. Treasury to work with Congress and provide taxpayers with clear guidance on how it intends to relieve double taxation arising from Amount A, and to engage with other jurisdictions that can be expected to relieve double taxation to provide clarity on the method through which double taxation arising from Amount A will be relieved.

USCIB members strongly encourage the United States to relieve the double taxation arising from Amount A by exempting the income reallocated under Amount A from U.S. tax. Members have identified several features of the existing U.S. foreign tax credit (FTC) regime that will need to be carefully considered to ensure the full relief of double taxation arising from Amount A, including U.S. source income rules, expense allocation rules, and previously taxed earning and profits rules.

Administration and compliance

USCIB members welcome the simplification and standardization of the administration and compliance framework for Amount A provided in the MLC. Members reemphasize that this simplification and standardization will be critical for Amount A to operate effectively. We look forward to the timely release of the Amount A Tax Return and Common Documentation Package so that our members can evaluate in greater detail the compliance obligations connected to Amount A.

Exchange of Information

The level of detail in the data required for calculations under the MLC is beyond any tax compliance regime in place in the world today. There are yet no clear guardrails to mitigate the risk that Amount A jurisdictions will not engage in “fishing expeditions” or that confidential taxpayer information improperly leaks over to non-Amount A jurisdictions. Further guidelines need to be developed to protect sensitive taxpayer information and to limit what is shared to information that is necessary for MLC compliance in the recipient jurisdiction. Also, more protective rules need to be in place where there are breaches of confidentiality, since there is such wide variation in the protections provided among parties in their domestic law, given the more sensitive nature of the data that is being incorporated into calculations under this MLC.

Tax certainty

While we believe that further work is needed to ensure tax certainty for tax administrations and taxpayers, we commend the novel and progressive approach to dispute *prevention* (the certainty element) and dispute *resolution* (the mutual agreement procedure (“MAP”) element) provisions contained in the MLC. These new elements can be attractive to business and can be incorporated on a “best practices” basis into the existing bilateral tax treaty framework and other dispute prevention and resolution mechanisms.

In our view, positive aspects of the tax certainty provisions include the creation and focus on advance certainty provisions that can provide forward-looking and binding multilateral certainty. The provisions were also designed to amplify the existing network of double tax treaties. The tax

certainty process also includes strict deadlines to ensure that inactivity on the part of one of the Parties to the Amount A MLC will not slow down and undermine the certainty process.

In contrast, the current dispute resolution and tax certainty provisions in the MLC can be further improved by ensuring that business has an active role in the dispute resolution process and providing access to certainty in the event of uncoordinated Amount A audits.

Composition of Determination Panels

Given the number of MNEs expected to be in scope for Amount A, there will be significant reallocations of U.S. MNE profits. There is likely to be frequent use of determination panels. The inclusion of non-governmental personnel on such determination panels could be inappropriate. The determination panel should be comprised of government officials from the ultimate parent entity lead tax administration, relieving jurisdiction, and market jurisdictions that are subject to government oversight. Appropriate panel design is key to the stability of the process and to the protection of sensitive and confidential taxpayer information shared as part of the process.

DST and relevant similar measures

As noted, one of the critical objectives of the Pillar One negotiation is to remove destabilizing and discriminatory tax measures that target U.S. companies. We appreciate this Committee's strong, bipartisan opposition to DSTs and other similarly targeted measures. Unfortunately, these taxes are becoming more common, and the MLC should ensure that DSTs are withdrawn. We also should ensure that they are not simply replaced by new discriminatory taxes that are designed through loopholes and ambiguous language. The MLC terms need to be clear that discrimination against non-domestic companies (including U.S. companies) will not be permitted.

We appreciate improvements made in the MLC text, including limiting loopholes like a *de minimis* exception to DST and relevant similar measures (RSM) designation or a proportionality limit, which would still permit discrimination. As mentioned in our U.S. Treasury consultation letter, however, we believe that further clarifications are needed to ensure that countries cannot use vague exceptions to push through discriminatory legislation.

Annex A to the MLC appropriately lists measures that have traditionally been considered DSTs. These measures should, of course, be withdrawn. There are some notable measures that are omitted. For example, the pending Canadian DST (discussed more fully below) is clearly of the same mold as the DSTs on the list and discriminates against U.S. companies.

The MLC should not enable countries to make a choice between Amount A and DSTs. The message from the U.S. should be that, while we are negotiating an agreement around allocation of taxation rights for certain profits, discrimination against U.S. companies should not be permitted in any case. That should never be a legitimate tax policy choice and is not simply a tax issue – discrimination through the tax system against U.S. companies is a trade issue. It must be clear, as USTR has done in the past with DST investigations, that countries who are found to act unilaterally, outside of an agreed upon framework of taxation rights, will be treated as inhibiting trade.

While our more specific recommendations are outlined in our U.S. Treasury consultation letter, let me mention a few points that we believe are of importance in achieving the goals of the MLC.

Article 39 of the draft MLC sets a threshold that, if measures "in practice exclusively or almost exclusively" target non-resident or foreign-owned businesses, the measure will be considered discriminatory. It is important that we are all aligned that these terms encompass both *de jure* and *de facto* discrimination. It is certainly our view that any tax measure that predominantly taxes non-resident companies, including business models that are predominantly from other countries, is discriminatory. That is what we are seeing happening to U.S. companies under DSTs. It is important that the term "exclusively or almost exclusively" is not defined too narrowly or else it simply establishes a loophole for further discrimination. Some clarifications, including perhaps some more instructive examples in the guidance, are needed to ensure the effectiveness of these provisions. Also, it is important to clarify that this measure could be based on tax revenues collected, not just the number of taxpayers. A few small domestic taxpayers should not be used as justification for targeted, substantial taxation of another country's companies.

We are also concerned about the level of subjectivity in the provisions in Article 39 that test if a measure is "insulating domestic businesses." There is an exception for "policy objectives," meaning that *de jure* or *de facto* discrimination can be permitted if it is tied to a permissible policy objective. Certainly, we believe that the intent behind this provision is narrow, but guardrails need to be added to the language to make that clearer and to set limitations. Excessive subjectivity or vagueness in setting exceptions will lead to loopholes that could undermine the fundamental objectives of these provisions. If those guardrails cannot be narrowly defined, we believe this exception should be deleted from the MLC text.

We applaud that the MLC text addresses significant economic presence provisions, although we believe there could be more clarity on the consequences for these measures.

Importantly, we have expressed our strong belief that the standstill agreement for DSTs be extended and were pleased to see that has been extended until the end of June. We are disappointed that certain countries have been grandfathered – that they are still allowed to collect DSTs from U.S. companies – but we believe it is important to avoid the proliferation of new DSTs as we are working out the terms of their withdrawal. We note, however, our disappointment that Canada has not respected the standstill and believe that their continued insistence on moving forward with discriminatory provisions puts the broader project of Pillar One at risk. One of our closest trading partners is moving forward with a discriminatory DST, including retroactivity which is particularly objectionable, and undercutting the stability and work of the OECD and the Inclusive Framework. We appreciate the letter that many members of this committee sent United States Trade Representative Tai and Secretary Yellen last September, and we ask that you continue to work closely with the administration to encourage Canada to rejoin the global consensus on DSTs.

Amount B

Amount B is considered a keystone feature of this overall project given the potential for it to deliver significant tax administration efficiencies for relatively standard transactions. Recently, Treasury publicly defined the agreement of a "robust Amount B" as a redline that must be

achieved before the MLC can be accepted by the United States.[2] Simply put, Amount B is a necessary and critical element of the overall Pillar One architecture.

Similarly, USCIB views Amount B as an important opportunity for business and tax authorities, especially in developing countries ("Low Capacity Jurisdictions" or "LCJs"), to work collaboratively to achieve much needed simplification within an international tax system that has become increasingly complex and fragmented. However, the proposed design of Amount B as described in the February 19, 2024 document released from the OECD still requires significant clarifications and revisions to achieve the stated objectives. In addition, and importantly, the path to widespread adoption by tax authorities and the broad application to taxpayers, including those in the scope of Pillar One, remains unclear.

To make the most of the tax certainty benefits of Amount B and enable widespread adoption, the drafters should strive for a broad spectrum of in-scope marketing and distribution activities, a pricing methodology design that is relatively simple to apply in practice by taxpayers and tax authorities alike, and multilateral implementation that is binding on all in-scope tax administrations and taxpayers. In this regard, we recommend:

- Increase the scope of Amount B to include a broad spectrum of industries and business models.

- Clearly define the list of initial low capacity jurisdictions that will be included within the scope of the initial phase of Amount B.

- Ensure that Amount B pricing approaches are economic in nature and consistent with current international norms for the allocation of profit for distribution activities.

- Establish that Amount B pricing approaches will be accepted by both market and principal jurisdictions; without this, Amount B will increase, rather than reduce, controversies, further burdening LCJ tax authorities.

- Limit the nature of complex qualitative assessment factors that determine if a taxpayer should be in scope of Amount B.

- Develop a clear and achievable timeline for completion of the Amount B design that can be broadly implemented in a binding manner.

We are concerned that the current design of Amount B falls short of the stated objectives of the OECD as well as the stated redline from the U.S. Treasury Department of a "robust Amount B." In our view, for Amount B to be effective as a stabilizing force in the international tax framework, the OECD and Inclusive Framework must continue their efforts to negotiate and ultimately agree upon an Amount B design that is acceptable to all stakeholders and broadly adopted globally.

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[2] Soong, Stephanie. "Amount B Tax Certainty Is a Red Line for U.S., Bello Says," Tax Notes." 12 Jan. 2024, www.taxnotes.com/tax-notes-today-international/oecd-pillar-1-profit-reallocation-digital-tax-repeal/amount-b-tax-certainty-red-line-u.s-bello-says/2024/01/12/7j2g1.

Closing

We believe in the value of our role to develop consensus positions of the U.S. business community that we contribute in detail to the development of these rules. Since the Pillar One solution was proposed, USCIB has offered practical solutions that will advance the design of the project underlying the MLC. We place a premium on offering specific guidance to the OECD which is shared simultaneously with the U.S. Treasury. We focus on generating guidance that will improve the workability of these novel sets of rules at the outset, if they are to take effect. Although we have not had a seat at the table in these years-long Inclusive Framework government negotiations, we can imagine a reality in which these rules can exist in some form in the interests of stabilizing the international tax system. We operate with urgency, as our goal in consultation is to promote the most workable version of these rules and we are well placed to do this.

We appreciate this Committee taking an active role in these important negotiations. We believe that any solution for U.S. companies must reflect the input of both the Biden administration and Congress, and we are encouraged by today's hearing.

In short, we believe that the *quid pro quo* for Amount A must be balanced for U.S. business. There needs to be reliable mechanisms to adjust and maintain that balance in order for business to make predictable investment decisions and to enable governments to collect taxes that are consistent with the economics of business operations. Amount B must be actively developed as best practice experience grows at tax administration and taxpayer levels. If developed and implemented correctly, Amount B can ensure an appropriate level of profit allocation to market jurisdictions, simplify tax compliance, and protect the tax base in the countries where significant capital investment and intellectual property creating activities take place. There needs to be a comprehensive solution to DSTs and other relevant similar measures within the MLC and for jurisdictions that do not sign up for the MLC. In addition, the interaction of Pillar One and Pillar Two taxes is a critical open question that must be addressed.

Thank you for this opportunity to testify today. This project is complicated and has a lot of moving parts over the next couple of months. We are at your disposal any further requests for discussion on these topics.