December 11, 2023

U.S. Department of the Treasury
Office of Tax Policy
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Re: NFTC Comments on the U.S. Department of the Treasury Request for Public Input on Draft OECD/G20 Inclusive Framework Pillar One Multilateral Convention Text

The National Foreign Trade Council (the "NFTC") is providing written comments on the draft Multilateral Convention to Implement Amount A of Pillar One (the "MLC") and accompanying documents published by the Organisation for Economic Co-operation and Development (the "OECD") on October 11, 2023, in response to the consultation launched by the U.S. Department of the Treasury ("Treasury").

The NFTC, organized in 1914, is an association of U.S. business enterprises engaged in all aspects of international trade and investment. Our membership covers the full spectrum of industrial, commercial, financial, and service activities. Our members value the work of the OECD and the Inclusive Framework ("IF") in establishing and maintaining international tax and transfer pricing norms that provide certainty to enterprises conducting cross-border operations.

General Comments

NFTC welcomes the consultation on the MLC and recognizes the efforts of Michael Plowgian and the rest of the Treasury team involved in the negotiations. We appreciate the opportunity to provide comments on a nearly complete draft of the MLC, and we appreciate the fact that the draft incorporates previous comments by the NFTC and stakeholders in response to prior consultations on components of the MLC.

The MLC represents a significant step forward in the effort to eliminate unilateral measures undertaken by several countries, thereby stabilizing the international tax system. While we recognize that any effort to renegotiate international taxing rights in favor of market countries will be complex, the complexity involved in Amount A, as reflected in the MLC in some cases leads to arbitrary results, and therefore may not achieve a durable stabilization of the international tax system. The Amount A mechanics, often provide results that are not intuitive or are otherwise unpredictable. This is further complicated by the numerous "cliff" effects in the MLC and explanatory materials, where dramatically different results can be achieved through small changes in inputs. We recognize that these mechanics are the result of negotiation among IF members. The proposed rebalancing of taxing rights must provide a durable stabilization of the international tax system to succeed.

Even with the significant progress made, numerous issues remain. Due to the number of outstanding issues, we are still considering whether we can support the MLC. We urge Treasury and the other IF members to resolve the outstanding issues in a manner that is principled, avoids undue complexity, and avoids double taxation.

Specific Comments

DSTs and Relevant Similar Measures

The revisions to the DST and relevant similar measures section are a welcome development. The enumeration of criteria will aid in deterring countries from using loopholes to implement destabilizing and discriminatory taxes.

We welcome the attention on significant economic presence (SEP) nexus rules in the provisions of Article 40, which ensure that a market country cannot apply SEP rules and the Amount A rules against the same Covered Group. However, we believe that SEP rules should be treated in the same manner as DSTs and relevant similar measures, and subject to the same standstill and withdrawal commitment to prevent the proliferation of SEP taxes.

We reiterate our request for a strong enforcement mechanism on the DST standstill. In some cases, Annex H(10) provides that Amount A is only denied following the date of a decision by the Conference of the Parties or otherwise starting with a period following the date on which the offending measure comes into effect. Instead, NFTC proposes that Amount A should be denied from the date such a law comes into effect. As the process for Pillar One will extend past 2023, we request that Treasury extend existing bilateral agreements with DST-imposing countries to coincide with the implementation of Pillar One. We also suggest that the MLC explicitly provide that Covered Groups paying DSTs should receive a credit against any Amount A liability in that jurisdiction until the DSTs paid are offset.

Article 39(2)(b)(ii)(A) and (B) defines a DST or relevant similar measure in part based on whether a measure applies restrictions that cause the measure to apply “in practice exclusively or almost exclusively” to non-resident or foreign-owned businesses and have the effect of insulating domestic businesses from the application of the measure. The narrow standard of “exclusively or almost exclusively” needs to be broadened to ensure that measures that are designed to fall predominantly (on the basis of tax collected rather than taxpayers in scope) on non-residents are disallowed. Instead of providing guidelines for implementing discriminatory policies, these destabilizing acts must be discouraged outright.

Discriminatory tax policy is destabilizing and, therefore, cannot be permitted. In the current explanatory language to Article 39(2)(b)(ii)(A), an example is provided where “only a few percent of the taxpayers” were domestic. We understand this is likely illustrative but fear it would be interpreted that a “few percent” may be acceptable – even if those few taxpayers represent insignificant tax collections or a large majority of tax collections are from non-resident or foreign-owned businesses that are part of Covered Groups based in other parties to the MLC. We recommend that the MLC and the explanatory statement provide that even some small domestic incidence of a discriminatory tax (e.g., 10% of collections from domestic companies) is not enough to shield a discriminatory tax from DST or relevant similar measure treatment where it is predominantly targeted at non-resident or foreign-owned businesses based in a particular country or in a particular industry.

Similarly, the flush language following Article 39(2)(b)(ii)(B) limits describes the “effect of insulating domestic businesses” standard in a problematic manner. Under the current verbiage, it appears that a tax with a clearly discriminatory impact could be salvaged by stated “policy objectives” that have an effect of insulating domestic businesses. Furthermore, it appears to create a requirement to prove discriminatory intent. Many countries have no or limited legislative history and thus, proving discriminatory intent is an unreasonable standard as policymakers will stand behind their stated policy objectives and not admit to de facto discrimination. NFTC proposes that the flush language following Article 39(2)(b)(ii)(B) should be deleted or restated as to not permit discrimination and/or destabilizing measures with this narrow standard.

Sourcing Rules

While the changes and simplification of the sourcing rules as recommended by the business community is a welcome development, unfortunately the rules are still extremely burdensome in some cases. For instance, the sourcing rules for other services (including cloud computing services) were helpfully revised to remove requirements that service providers request additional data from their customers. The reliance on commercial and other available information rather than novel reporting obligations is a step forward. However, we request examples of how to navigate the rules in cases where data for enumerated reliable indicators is unavailable.

Another change provides that customers of other services should be segregated into three categories (Small, Large, and Resellers). In theory, separating customers into three buckets and applying a tailored allocation method seems logical. In practice, applying different allocation methods may require information not routinely contained in systems or obtained from customers as a matter of course.

Using three sourcing rules will require Covered Groups to split revenues between direct customers and resellers, which imposes a large administrative burden and significant complexity. At times, customers are also resellers, which would require segregating the revenues between those which relate to the seller as a customer versus those which relate to resale transactions in order to apply the different sourcing criteria. This is seemingly impractical and, in some cases, impossible. For some members, the provider could have thousands or even a million different accounts, and a single customer may have multiple accounts which are not linked. The rules should allow Covered Groups to affirmatively use the same allocation key method for all three categories of customers, for example the address of the immediate service recipient, where the relevant information to segregate is difficult to obtain.

The headcount allocation used for Large Customers is particularly problematic as it requires a different allocation to be applied for each location that the Large Customer has their headquarters. This is not practical and is overly burdensome. Covered Groups would need to segregate their customers into a subset of Large Customers and then obtain customer-specific information as to those customers’ headquarters locations. Some of this information is not public data, resulting in compliance delays by the filing group as they gather the data and subsequently determine the appropriate allocation key. Any requirement to examine a client file in multiple contexts would particularly be difficult due to the uncertain requirements needed to demonstrate that the Covered Group has reviewed all information related to a customer (for example, decentralized files of sales personnel) in any employee’s possession. Additionally, the linkage of such aggregated headcount data to the sourcing of services performed is unclear.

The embedded complexities in the sourcing rules are an example of why compliance for Amount A will be arduous and require ongoing maintenance and analysis for even the most sophisticated taxpayers. Furthermore, even with the recent modifications, the sourcing rules may still require businesses to request information from third parties, which they need to integrate into their IT systems. As a result, the sourcing rules are one example supporting the need for a transition period, ideally a minimum of two years, for the MLC to come fully into effect after the ratification threshold is met.

De Minimis Threshold

The threshold for an Amount A allocation is €1 million for a market jurisdiction (or €250,000 in the case of a low-GDP jurisdiction). While well intentioned, as noted in the discussion of the MDSH at their current values the *de minimis* thresholds for Amount A are of little practical benefit. One member noted that the thresholds eliminated fewer than ten jurisdictions from their Amount A calculation. Further, the Amount A liability for some Covered Groups is minimal (under $50,000) in many jurisdictions for which an Amount A determination is required, especially given the compliance burden to arrive at that amount. We suggest that the IF provide Pillar One estimates and determine if the compliance burden involved in the reallocation is warranted, given the small economic impact to market jurisdictions. We recommend that the *de minimis* thresholds be increased to at least €10 million in revenue or measured via a minimum level of tax due in a market jurisdiction (for example, at least €50,000).

Transitional Segment Rule

The transitional segmentation rule provided by Section 4(2) of Annex C is problematic. As drafted, the rule would require a multinational group to calculate Amount A as a segment in the first year in which the group is a Covered Group rather than allow the calculation as a Covered Group. We recommend that the revised MLC disregards the segmentation approach in any year in which the Covered Group is in scope. There is no basis for treating two otherwise comparable Covered Groups differently solely because one of the Covered Groups had an in-scope “Covered Segment” in a prior year. If this provision is included as currently drafted, then a corresponding reduction in Amount A is needed for any year following that in which a Covered Group falls out of scope.

Adjustment for Withholding Taxes

The business community appreciates the incorporation of our prior feedback to provide a mechanism to account for withholding taxes imposed by a market jurisdiction, which reduces the Amount A allocation to that market jurisdiction. Despite the adjustment mechanism, we are apprehensive about its effectiveness in practice which will lead to double taxation. While we requested a dollar-for-dollar adjustment for withholding taxes based on the principle that the same profits should not be subject to tax twice by the market jurisdiction, we understand that limiting the withholding adjustment to less than 100% of the tax paid was needed as a political compromise. However, we are concerned that this compromise did not encompass a broader agreement on withholding taxes, which is highlighted by the number of reservations in the MLC related to the treatment of these taxes. We are further concerned that anything short of a dollar-for-dollar adjustment for withholding taxes will have the perverse effect of endorsing existing withholding taxes on income such as royalties or service fees or even encouraging the introduction or increase of such taxes, in contravention of long-standing U.S. policy. As the current mechanisms do not cap market allocations, novel avenues of increasing revenue without impacting the Amount A allocation may develop. We urge Treasury at a minimum to preserve the progress that has been made on this issue, and to redouble its efforts, together with those of like-minded IF members, to achieve a dollar-for-dollar adjustment for withholding taxes.

Marketing Distribution Safe Harbor (MDSH)

The MDSH still needs refinement before finalization, as well as assurances for stability. We are concerned that many of the design elements are not based on economic principles and are seemingly arbitrary. We request that the OECD provide rationale as to the returns and adjustments chosen, including the Elimination Threshold and the Jurisdictional Offset Percentage. Without ties to an economic principle, these variables are seemingly arbitrary, thereby making them susceptible to future adjustments. It would be difficult to obtain the goal of stability if these values are subject to future adjustment. This is particularly consequential given the recent UN resolution and the potential for changes made outside of the IF (e.g., at the UN). We also request adjustments that recognize the cyclicality of businesses with resultant reactions to economic trends.

As an example, one of the key variables in the MDSH calculation is the "Jurisdictional Offset Percentage." This percentage has the effect of reducing the potential amount of the MDSH reduction applied to market jurisdictions (and also reducing the overall amount of Amount A to be surrendered from relieving jurisdictions). Under the MDSH formula, the higher the Jurisdictional Offset Percentage the more Amount A profits are eliminated from the overall Amount A calculation. The baseline Jurisdictional Offset Percentage established by the MLC is 35%. For certain low-income jurisdictions, the offset percentage is established at 25%. For jurisdictions with low functional intensity, the offset percentage is established at 90%. Similar to other variables in the MDSH, these percentages appear to be arbitrary in their creation and future adjustment of the variables would significantly impact the stability of the overall Amount A mechanics. We request that Treasury or the OECD provide a rationale for the offset percentages included within the draft MLC.

The *de minimis* threshold contained in the MDSH is low and unaligned with the *de minimis* threshold for the imposition of Amount A. The MDSH *de minimis* threshold is €50 million, whereas the threshold for an Amount A allocation is €1 million for a market jurisdiction (or €250,000 in the case of a low-GDP jurisdiction). The result is that there are many jurisdictions that will impose Amount A, but where the MDSH will not be available. As noted elsewhere, the low threshold for applying Amount A will lead to a significant compliance burden for Covered Groups in proportion to the revenue affected. Therefore, NFTC requests that the threshold for Amount A be increased to align more closely with that of the MDSH. Furthermore, NFTC members believe the scope of the MDSH should include intangible goods and services that are increasingly significant in transactions across the vast array industry sectors which comprise the global economy.

The MDSH defines normal or routine profit as the higher of (1) marking up the jurisdiction's depreciation and payroll by a ratio equal to ten percent of the Covered Group's sales over depreciation and payroll; or (2) three percent of adjusted jurisdictional revenues. We want to highlight that in some instances, the return in a market jurisdiction determined under traditional transfer pricing may be below the formulaic returns determined under the MDSH. We are concerned about creating an incentive for a tax authority to audit a Covered Group's operations and increase taxable income outside of Amount A up to the level of the Elimination Threshold. This may allow jurisdictions to collect additional revenue (irrespective of the arm's length principle) without impacting their guaranteed Amount A allocation. In order to safeguard against this, we recommend mandatory implementation of Amount B as an optional safe harbor on which Covered Groups can rely. We also encourage Treasury to expand the existing network of tax agreements to allow for broad access to MAP and other dispute resolution mechanisms.

Double Taxation

The threat of double taxation continues to loom and needs to be mitigated. The MLC provides limited assurances that the obligation to relieve double taxation will be fully satisfied. We are also concerned that the alternative mechanisms proposed to relieve double taxation may not work as seamlessly as envisioned including integrating with existing domestic tax regimes. We request the provision of further guidance to ensure full relief from double taxation on any Pillar One tax liability. We reiterate our request that Treasury provide guidance on the envisioned interaction of Pillar One (and Pillar Two) with our existing rules, including rules providing for correlative adjustments in the case of reallocations of income, rules providing for foreign tax credits with respect to additional foreign taxes imposed on foreign source income, and GILTI rules.

We continue to recommend the elimination of double taxation via exemption. The significant flexibility in the MLC which under domestic laws that may contribute to double taxation. An example is relief afforded via carryforwards of credits for a minimum of three years, without any clarity on what happens if relief is not achieved after three years. The MLC should not preempt any relief of double taxation available through other avenues.

We strongly urge that Amount B is mandatory for all jurisdictions and provided as an optional safe harbor for all Covered Groups in scope of Amount A. The scope of Amount B should be broadened to all distribution and similar activities, including distribution in relation to services and digital property, with no "ring fencing" of distribution activities or exclusions (e.g., for local comparables). Amount B should be implemented prior to Amount A. This would provide tax certainty for tax administrators and Covered Groups with regard to Amount B calculations prior to the overlay of Amount A.

We understand that the integration of Pillar One and Pillar Two will be part of the Pillar Two discussions. Several clarifications are needed including an ordering rule and confirmation that Pillar One tax should be treated as a Covered Tax in the relieving jurisdiction rather than the jurisdiction of the Designated Payment Entity. Clarifications as to whether GloBE income adjustments are necessary to incorporate the surrender effects of Pillar One calculations is also needed.

The Return on Depreciation and Payroll tiers based upon 1500% and 150% create a potential cliff effect in the Amount A formula. The avoidance of a cliff is recommended when possible. Furthermore, if the negotiated thresholds are retained, assurances should be given that these cannot be changed in the future. Fluctuations in the parameters of the Amount A formula will lead to financial uncertainty for Covered Groups and their investors. We also note that the interdependency of the Amount A calculation variables may result in unintended financial outcomes that are not directly tied to business operations in a particular jurisdiction. For example, the standard return for routine manufacturing and/or distribution activities will be influenced by overall group profitability, return on depreciation and payroll across other jurisdictions, etc. Tax effects of transactions or business decisions are generally determined by the results of the Controlled Group as a whole and are not limited to one or two jurisdictions.

Tax Certainty & MAP

Tax certainty is a central tenet of Pillar One. We applaud the efforts by Treasury and the IF to provide mechanisms to allow such certainty with respect to Amount A and related matters. Article 22 works in conjunction with Article 23 allowing Covered Groups to request advanced certainty. We are concerned that in year one a majority of Covered Groups will submit a request under one or both of the provisions and may overwhelm the system. In order to mitigate the tsunami of requests, we suggest that either a pilot program is launched for these requests and/or a sufficient window is provided prior to the MLC coming into effect to allow Covered Groups to obtain the advanced certainty.

The novel concepts in the MLC MAP provisions require either an existing bilateral tax treaty or both parties to be signatory to the MLC. There are instances of major trading partners not having a bilateral tax treaty or potentially not signing the MLC (such as is the case for the U.S. and most Latin American countries) and as a result there may be no access to the dispute resolution MLC provisions. Full and comprehensive tax certainty should be an objective of all tax administrators despite gaps in the bilateral treaty networks or MLC implementation.

It is imperative that the MLC provide equal access to all tax administrators and Covered Groups for tax certainty for related issues. NFTC continues to advocate for countries, particularly the United States, to build upon their existing networks of bilateral tax treaties. We further suggest that a baseline of transfer pricing guidelines be employed where a bilateral agreement is not in effect for purposes of Article 33.

The progress made on mandatory binding resolution is commended. Particularly helpful is the expansion of definition for "matters related to Amount A" that now includes Transfer Pricing, Permanent Establishment and Withholding tax disputes, at least where the dispute is otherwise within the scope of a covered tax agreement. By expanding the scope, tax certainty for Covered Groups increases which leads to greater stability of the international tax system. We note again that the United States has a relatively narrow network of tax agreements as compared to other countries; for example, the United States does not have tax agreements covering Singapore, Hong Kong, most of Latin America, and most of Africa. This relatively narrow network puts the United States at a competitive disadvantage and may reduce the benefits of the dispute resolution mechanisms being developed by the IF. We urge Treasury to recommit itself to negotiating tax agreements with significant trading partners to bring additional transactions and arrangements under these dispute resolution mechanisms, and further pledge the NFTC's continued support for these efforts.

As envisioned, the tax certainty user fee is unnecessarily burdensome. We also suggest the addition of a mechanism to permit coordinated reviews that allow for coverage of multiple items with a set fee as opposed to a user fee on an issue-by-issue basis.

The rules regarding the expiry of the two-year bilateral phase of the MAP includes following statement:

> The start date for this two-year period is determined pursuant to paragraph 6 or 7, as the case may be. The MAP competent authorities may, however, agree to a different time period with respect to a particular case, provided that they notify the member of a Covered Group who presented the case of such agreement prior to the expiration of the two-year period referred to paragraph 1(a)(ii).[1]

We request that a binding timeline is created to ensure disputes are timely resolved. The ability for MAP to extend a timeline without a clear timeframe and no consent required by the Covered Group will exacerbate uncertainty. As Treasury is aware, tax disputes in foreign jurisdictions can take years or even decades to resolve. Consent of the Covered Group should be required for any material extension of the

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[1] Organization for Economic Co-operation and Development, *Explanatory Statement to the Multilateral Convention to Implement Amount A of Pillar On*e, Article 35 - Resolution of Disputes with respect to related issue*s,* Paragraph 795, 186 (2023) available at: https://www.oecd.org/tax/beps/explanatory-statement-multilateral-convention-to-implement-amount-a-of-pillar-one.pdf

timeline. Once the dispute has continued for that timeframe, Parties should move toward engaging the dispute resolution panel. If this provision is maintained, there should be parameters imparted which respect the overall goal of expeditious resolution.

Without such a timeline, uncertainty will become widespread due to the layers of impacts contained Pillar One and Pillar Two. The result will be the inability to comply with the complex sets of rules that govern Pillar One and Pillar Two calculations. (This will be in addition to any domestic tax requirements that also need to be taken into account as a result of any adjustments.)

The MLC contains several instances where the verbiage suggests that jurisdictions may disregard the rules.[2] Covered Groups have no alternative routes to engage in dispute resolution procedures, explain their conclusion, or otherwise resolve the relevant related issues should the issue be disregarded by the competent authorities. In the spirit of encouraging dispute resolution and stability, these references should be removed. Furthermore, thorough review of the provisions which ensures that certainty approaches are designed to enable broad certainty to all material aspects of the Amount A calculation should be undertaken. Competent authorities should have narrowly tailored exceptions that allow them to decide to exclude items relevant to Amount A from the certainty processes. If such offending provisions are retained, a requirement to engage in some dispute resolution process (presumably more suitable to the Parties) to ensure resolution and the avoidance of double taxation must be added.

Other Issues

Additional clarity is needed for the Currency Conversion Rules in Article 21. As Parties are given the flexibility to use their own exchange rates where there are "legal or practical impediments" how does this coordinate with the thresholds? How are disputes over a threshold handled? We recommend the addition of a default rule governing conversion rate to mitigate disputes over thresholds resulting from the flexibility.

In convening a Determination Panel under Article 27, one of the options presented should be the Covered Group's approach. Failure to consider the Covered Group's approach may lead to unfair determinations and additional litigation.

Sensitivity of taxpayer data remains a concern of the business community. Due to the detailed calculations required for the MLC, Treasury should work to reign in the current standard of "foreseeably relevant" for Exchange of Information in Article 37, which is far too broad. The acknowledgement of prohibiting requests for information for fishing expeditions is appreciated, but clear guardrails must be set into place to mitigate distribution of sensitive taxpayer data. We request more transparency on exchanging data to conduct "tax policy analysis." If this entails anything beyond sharing routine aggregated data with the OECD for tax statistics, we would object to the provision. Strong guidelines need to be developed to protect sensitive information and to limit data to only the information which is absolutely necessary for compliance with the MLC. Deterrence and protective measures must be put in place for any breaches of confidentiality, since Covered Groups cannot rely on each country's domestic protections.

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[2] *Id.* at Paragraph 848, states:

Although the Convention does not provide for general exclusions from the scope of the dispute resolution panel process in Article 35, paragraph 10(b) allows MAP competent authorities to **mutually agree to exclude from the scope of the dispute resolution panel process cases that are not suitable for the dispute resolution panel process in their common view** on a case-by-case basis. [Emphasis added]

In Annex B, Calculation of Adjusted Profit Before Tax, Tax stock-based compensation (SBC) is taken into account in Elimination Profit (Annex B, Section 4(2)), but it is not taken into account in Adjusted Profit Before Tax (Annex B, Section 2(1)). We request that these standards are aligned to take tax SBC into account in the calculation of Adjusted Profit Before Tax.

In Annex H - Subnational Jurisdictions, the rules do not provide a denial of Amount A denial for countries in which subnational governments impose DSTs. Failure to close this loophole will encourage the proliferation of subnational DSTs. We suggest providing a requirement that the jurisdiction must act and to allow for some alleviation of the impact of the destabilizing measure against the Amount A liability at the national level. Without such a remedy, DSTs may simply proliferate at the subnational level with no incentive by the parent jurisdiction to act.

Conclusion

While we appreciate all of the progress made on the MLC, several important outstanding issues remain. We recommend that these issues continue to be addressed by Treasury and other IF members. Due to the number of outstanding issues, we are still considering whether we can support the MLC. We urge Treasury to continue working with the OECD and IF counterparts to resolve the outstanding issues in a manner that is principled, avoids undue complexity, and avoids double counting or double taxation of the same income. We believe that any negotiated outcome that falls short of these objectives will ultimately fail to bring stability to the international tax system.

The continued engagement with the business community on the IF is welcome. We are happy to answer any questions or provide clarification on any of the issues raised.

Sincerely,

Anne Gordon
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National Foreign Trade Council