Holland & Knight

800 17th Street N.W., Suite 1100 | Washington, DC 20006 | T 202.955.3000 | F 202.955.5564
Holland & Knight LLP | www.hklaw.com

Joshua D. Odintz
+1 202-469-5207
Joshua.Odintz@hklaw.com

December 11, 2023

*Via E-mail (OTP_Pillar1MLC@treasury.gov)*

Secretary Janet Yellen
U.S. Department of the Treasury
1500 Pennsylvania Ave., NW
Washington, DC 20220

Re: Comments on OECD/G20 Inclusive Framework Pillar One Model Convention Text

Dear Secretary Yellen:

The Principled Pillars Coalition (PPC) is providing these comments on the draft Multilateral Convention to Implement Amount A of Pillar One, published on October 11, 2023 (the MLC) and the accompanying documents.

The PPC is an ad hoc coalition of multinational businesses that would like to see Pillar One succeed to provide tax certainty for its members and governments. The PPC is comprised of both inbound and outbound multinational enterprises that undertake a wide range of activities, from financial services to manufacturing and sales to consumers.

The PPC thanks Treasury for the opportunity to comment on the MLC. The MLC and associated commentary are complex and have changed since the business community saw many of the modules over the last two years. Accordingly, Treasury should provide additional time to comment. The Organisation for Cooperation and Development (OECD) and Inclusive Framework should also provide a comment period for the complete MLC package, as they made several substantial revisions to the draft rules, including changes to the treatment of withholding taxes.

We support a solution to digital service taxes (DSTs) and other bespoke taxes that are designed to bypass income tax treaties. The PPC supports an MLC that simplifies the approach to Amount A and provides tax certainty to both taxpayers and tax administrations.

**The MLC Should be Revised to Address Decentralized Businesses**

The members of the PPC have a common fact pattern – they are all decentralized groups. The MLC operates best where a multinational enterprise (MNE) has one or two centralized businesses. The reality is quite different. An example illustrates the complexity of applying the MLC to a decentralized business.

Large Co is a publicly traded MNE that manufactures several components for numerous uses and industries. Large Co also manufacturers goods for sale to consumers, primarily through third party retailers. The company provides services for some of the components and for goods for sale to consumers, including service contracts. Large Co operates in a decentralized manner and is comprised of over 100 separate business lines. Each business line has its own management. Large Co started some of the businesses, while it acquired others over the last 30 years.

Financial reporting systems allow Large Co to prepare consolidated financial statements at the parent level for reporting to the Securities and Exchange Commission. However, the financial reporting systems do not report to the ultimate parent entity each sale at the subsidiary level in foreign countries. Tax filing obligations are addressed by each entity or combined group in each country. Large Co's ultimate parent entity currently does not have the information regarding each foreign transaction to allow for resourcing of the various sales and services provided to businesses and consumers.

The PPC's comments are provided against this background.

**Pillar One Should be Delayed Until At Least 2030**

The PPC recommends delaying the implementation of the MLC until at least 2030 in order to provide jurisdictions and taxpayers opportunity to program and prepare for the significant changes contained in the MLC.

Many governments are still implementing the action items from the OECD's Base Erosion and Profit Shifting Project (BEPS 1.0). Pillar Two is in the process of being translated into local law. More than 50 countries will implement all or part of Pillar Two over the next three years. Contrary to prior pronouncements, the Pillar Two rules are not stabilized. The OECD will publish additional administrative guidance by the end of the year, as well as additional guidance in 2024 and beyond. The OECD will need to issue subsequent administrative guidance on the extension of the various safe harbours (e.g., country-by-country safe harbour, qualified domestic minimum top up tax safe harbour), and the numerous additional issues raised by stakeholders. Further, Pillar Two will create significant tax disputes, and to date, Pillar Two lacks a special dispute resolution mechanism. We anticipate numerous multilateral disputes if the undertaxed profits rule is implemented. Both business and governments will need significant resources to implement Pillar Two and address such tax disputes.

Adding the MLC in the short term would create tremendous pressure on both governments and MNEs. Governments will require additional resources to handle the multilateral disputes that will arise from Amount A and issues related to Amount A. Dispute resolution for issues related to Amount A will require significant government resources. As an example of the resources required in the United States, the average time to complete a bilateral advance pricing agreement (APA) is 53 months for a new APA, and 36.6 months for a renewal.[1] While APAs are time intensive, they are also collaborative and require cooperation from the taxpayer. The APA statistics illustrate the need to continue to increase staff at APMA, and other governments will need to increase and train their staff.

The burden the MLC will place on business cannot be understated. Unless the MLC is simplified, taxpayers will need to hire and make significant investments to allow for the centralized collection of information on all sales of goods and services. The costs and impact will be more pronounced for decentralized businesses, where different business lines operate independently. Third-party contracts will need to be renegotiated to provide information required to resource millions of transactions. The costs for business will be substantial. As an illustration, the costs of Foreign Account Tax Compliance Act (FATCA) compliance exceeded $574 million for a 10-year period. FATCA is a narrow law that imposed reporting requirements on financial institutions.[2] The changes proposed in the MLC are sweeping and fundamental and will require MNEs to make significant investments to comply.

In light of these significant changes and burdens, the MLC should apply to tax years beginning in 2030.

**The Scope of Amount A Should be Reduced, Which Will Lead to Simplicity**

The complexity of Amount A is significant in part because of the Inclusive Framework's expansion of Pillar One to include business-to-business (B2B) transactions. Originally, the Pillar One Blueprint (Blueprint) [3] was limited to certain activities: automated digital services and consumer facing businesses. Component part supplier and manufacturers, or B2B transactions, were excluded.

[1] See Internal Revenue Service Announcement 2023-10, https://www.irs.gov/pub/irs-drop/a-23-10.pdf
[2] Treasury Inspector General for Tax Administration report number 2022-30-019 (Apr. 7, 2022).
[3] 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, https://doi.org/10.1787/beba0634-en

The Blueprint discussed whether and how to address dual use intermediate products and components. The Secretariat was concerned with administrability and a simpler compliance approach:

> The alternative would be to include in scope even the sale of component parts to businesses on the basis that sometimes they can be directly acquired by a consumer. This would be a significant compliance burden, and would require difficult revenue sourcing rules to be developed. This is because a component part when sold to a business would then need to be traced through what may be a complex supply chain. For example, in the case of a car tyre, this may be shipped to the location of the factory where all tyres are stored, to the factory where the cars are assembled and further manufactured, and through the distribution channel to locate the place where the tyre is ultimately sold to a consumer as part of the car. Instead, the obligation would only be to source those sales made to consumers, which should be feasible because of the different nature of the product when sold to consumers, as noted above.[4]

The MLC does not take this approach. Rather, it creates a complex tracing requirement for all components that will require all businesses to reprogram their systems to satisfy the sourcing rules. The costs to comply will be material; yet it is unclear whether such changes will result in more tax revenue for market jurisdictions.

A simpler approach is to remove components and dual use intermediate products. Further simplicity can be achieved by removing all B2B transactions from Amount A.

The PPC also recommends modifying and expanding the exemption for Regulated Financial Institutions (RFI) in two ways. First, as drafted, the MLC exempts three-party payment systems but does not exclude four-party payment systems. An open-loop or four-party payment system operates as a service provider between issuing banks and acquiring banks. The core activities are authorization to verify individual transactions, clearing electronic instructions on batch transfer of funds, and settlement by the batch transfer of funds. In contrast, three-party payment systems (aka closed-loop) offer issuing and acquiring services, i.e. they sit on both sides of the transaction with consumers and merchants.

Failure to include four-party payment system operates in the RFI exemption will create market distortions. Three-party payment systems likely qualify for the RFI exemption, the Autonomous Domestic Business Exemption, or as exempt government entities.

The RFI should be expanded to permit authorization, clearing and settlement services provided by electronic payment service providers whether performed by third parties or by an RFI.

---

[4] *Id.* at 46. Note some countries advocated for this simplifying convention, while one country wanted to include all dual use intermediate products and components.

The PPC also recommends modifying the definition of Insurance Institution to include insurance brokers. Specifically, the definition of Insurance Institution requires an entity to satisfy a licensing requirement, a regulatory requirement, and an activities requirement.[5] Insurance brokers satisfy the licensing requirement and regulatory requirement, but the scope of activities is limited to revenue from the issuance of insurance contracts. In many instances, large insurance brokers manage the general underwriting services for an insurer. The definition of activities should be expanded to include insurance brokerage activities.

**Withholding Taxes**

The PPC agrees withholding taxes should offset the allocation of Amount A to market jurisdictions. Withholding taxes are another method for countries to tax extraordinary returns generated elsewhere. The PPC advocates for full recognition of such taxes paid against the Amount A allocation.

The PPC recognizes some countries disagree with the design of the withholding tax uplift. We assume these countries want to lower or eliminate the application of withholding taxes against Amount A. Failure to provide a full Amount A offset for withholding taxes will incentivize market jurisdictions to impose new and higher withholding taxes on a variety of cross border payments. Those jurisdictions that impose additional withholding taxes will double tax some portion of the Amount A allocation. A discount on the amount of withholding taxes creditable against Amount A will reward such conduct.

The MLC is premised on the removal of distortive digital service taxes and similar measures, the failure to provide a dollar-for-dollar credit for withholding taxes against Amount A would create a new category of distortive taxes.

**Expense Allocation**

The MLC would shift 25 percent of extraordinary returns to market jurisdictions. Under this approach, market jurisdictions will enjoy greater returns without the associated costs to generate such returns. The PPC members invest in plant, property, equipment, research and other significant expenses to bring products and services to market. The non-routine returns reflect risk, and the profits of such investments will be shifted in part to jurisdictions that are not sharing in that risk.

Related costs should be allocated to market jurisdictions to reflect the shifting of risk. Unless a proportionate amount of expenses is allocated to the jurisdictions that receive an Amount A allocation, Amount A will operate as a heads I win tails you lose methodology for market jurisdictions.

---

[5] MLC Commentary at para. 1762-1773.

**Dispute Resolution Must Be Mandatory**

The PPC supports innovative dispute resolution matters that will provide certainty for both governments and taxpayers. The MLC would provide options for three types of certainty reviews: scope certainty, advance certainty, and comprehensive certainty. The innovative form of arbitration through rank choice voting based on presented alternatives is an excellent process to create tax certainty.

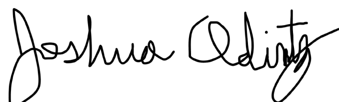
Further, the PPC supports mandatory binding dispute resolution for issues related to Amount A (Related Issues). Related Issues include transfer pricing, permanent establishment, and withholding tax issues. We make the following observations and requests regarding the process for Related Issues. First, the process is elective for certain jurisdictions, which will result in a failure to reach a resolution on key issues that will affect the Amount A calculation.[6] Related Issues for in scope MNEs should be resolved through binding arbitration, regardless of the size of the country. Second, many countries that have existing tax treaties routinely deny access to the mutual assistance program (MAP) under an applicable treaty. In some instances, countries treat a transfer pricing adjustment as a criminal matter but will convert it to a civil matter so long as the taxpayer agrees to forgo MAP. The MLC should affirm that taxpayers have an automatic right to MAP for Related Issues.

Third, a Related Issues dispute can access the MLC MAP after two years. However, the Competent Authorities can agree to extend the timeline for access to MAP without consent of the taxpayer and for a period without an upper limit.[7] A significant delay in resolution of Related Issues will affect the Amount A calculation and undermine tax certainty. The MLC should include a rule that the MLC MAP provisions will apply automatically after two years. This will encourage Competent Authorities to timely resolve Related Issues.

**Conclusion**

We thank Treasury again for accepting comments on this momentous proposal. We welcome the opportunity to meet with you to discuss these comments and related issues.

Sincerely yours,



Joshua D. Odintz

Counsel to the Principled Pillars Coalition

[6] MLC Article 36.
[7] MLC, Article 35(1)(a)(ii).

cc: Lily Batchelder, Assistant Secretary, Office of Tax Policy, U.S. Department of the Treasury

Michael Plowgian, Deputy Assistant Secretary (International)

Lindsay Kitzinger, International Tax Counsel

James Wang, Deputy International Tax Legislative Counsel

Elena Virgadamo, Deputy International Tax Legislative Counsel

Beth Bell, Senior Advisor

Huzefa Mun, Attorney-Advisor

Peter Blessing, Associate Chief Counsel (International)