



Memo

To Tax Treaties, Transfer Pricing and Financial Transactions Division,
OECD/CTPA

From KPMG International

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Ref Comments on the Public Consultation Document for Pillar One – A
Tax Certainty Framework for Amount A

Professionals in the member firms of KPMG International¹ (“KPMG”) welcome the opportunity to comment on the OECD’s public consultation document entitled “Pillar One – A Tax Certainty Framework for Amount A,” released on 27 May 2022 (the “Consultation Draft”), as well as its companion public consultation document titled “Pillar One – Tax certainty for issues related to Amount A,” released on the same date (the “Related Issues Draft”). This comment letter responds specifically to the Consultation Draft but should be understood in the context of our comments on the Related Issues Draft, which have been submitted under separate cover.

The design of Amount A represents a significant change to the way the international corporate tax system has operated for the past hundred years, providing jurisdictions with a taxing right over the profits of in-scope Multinational Enterprises (MNEs) calculated using a single global formula. To ensure a MNE’s profits are subject to tax once, the Amount A rules must be applied in the same way in each jurisdiction that adopts Amount A and new procedures must be established to prevent double taxation. For this reason, the tax certainty framework is a critical part of Amount A, and we commend the Inclusive Framework for the focus on this issue.

The Inclusive Framework’s October 8, 2021 “Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy” (the “October Statement”) announced a historic commitment to tax certainty through mandatory and binding dispute prevention and dispute resolution for both the determination and allocation of Amount A and Related Issues associated with Amount A.² While we understand that some jurisdictions have expressed concern about whether the certainty process would impinge on sovereignty, we believe that the certainty process (including certainty for Related Issues) is

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² Capitalized terms not defined herein have the meanings assigned to them in the Consultation Document and the Related Issues Draft.

fundamental to sovereignty by seeking to preserve the integrity of each jurisdiction's choices in reaching an agreement with respect to multilateral taxation and ensuring the durability of that agreement.

The following comments do not aim to be comprehensive, but rather focus on select areas to improve the tax certainty framework set forth in the Consultation Draft.

Advance Certainty

Although the Consultation Draft provides for an Advance Certainty Review, we believe the benefits of this process could be further enhanced by expanding its scope and establishing fixed deadlines to ensure that this process concludes before a Group is required to file its Amount A return. The rationale for these proposed changes is outlined below.

First, the Advance Certainty Review should be extended beyond revenue sourcing and segmentation issues. The entire Amount A allocation framework – including elimination of double tax, the marketing and distribution profits safe harbor, and the effect of withholding taxes – should be addressed on an advance basis through agreement on the methodologies that the Group will apply.³ Preventing disputes from arising, rather than seeking to resolve them once they have arisen, maximizes certainty and promotes efficiency for both tax administrations and taxpayers. The International Compliance Assurance Programme (“ICAP”) and Advanced Pricing Agreement (“APA”) programs provide models that we encourage the Inclusive Framework to look to in designing the Advance Certainty Review. We also encourage the Inclusive Framework to consider how the Advance Certainty Review can be designed to address the shortcomings of existing programs (e.g., long resolution periods for APAs). As work continues on the remaining building blocks, consideration should be given to designing rules that would facilitate advance certainty, consistent with the commitment set forth in the October Statement.

Second, the Advance Certainty Review should include strict time limits to ensure that certainty can actually be provided on an advance basis. In some places the certainty processes described in the Consultation Draft are unclear and have undelimited timing, which could prevent the process from being completed before a Coordinating Entity is required to file the Group's Amount A return. We believe that a 24-month Advance Certainty Review taking place during the two years leading up to a Period (following an initial transitional period for the earliest years of Amount A's application) would provide appropriate time for the requisite review and panel processes. Consistent with the approach envisioned by the Consultation Draft, this Advance Certainty Review would provide certainty for multiple years. If an Affected Party disagrees with a Review Panel recommendation after a set period (e.g., after 21 months of the 24-month period) has lapsed, the case should proceed immediately to a Determination Panel (with the disagreeing Party's position as one of the potential resolution choices). This would ensure that certainty is provided to tax administrations and taxpayers in a timely manner.

These improvements are not only technically achievable, particularly taking into account the formulary nature of Amount A; they are necessary if the tax certainty framework is going to achieve its aims, especially once the number of in-scope MNEs is expanded. Certainty considerations have ramifications beyond individual Groups:

³ We note that the determination of whether an enterprise is in scope for Amount A is a different process that is less reliant on company systems and incorporates current Period facts and financial results.

tax expenses are a significant financial reporting item, and uncertainty with respect to Amount A liabilities for the largest companies in the world could have significant effects for capital markets.

Advance certainty is also crucial to ensuring that dispute prevention can be achieved in an effective manner. It has been our consistent experience that tax administrations are more able and more willing to compromise with their counterparts in APA discussions than in mutual agreement procedure (“MAP”) negotiations, when tax has already been paid and one tax administration is faced with the prospect of granting a refund. Agreeing in advance on methodologies makes it easier to reach a principled resolution that is less directly tied to fiscal considerations, and providing a broad Advance Certainty Review process for Amount A would facilitate more expeditious and effective resolutions.

Transition

With Amount A expected to become effective in 2024, it will not be possible to complete an Advance Certainty Review on the 24-month timeline suggested above before the first year for which Amount A will be due. Accordingly, a transitional period will be necessary. As noted in the Consultation Draft, a transitional period will also be crucial to providing certainty as Groups adopt systems to apply Amount A. In the transitional period, Groups should be allowed to apply reasonable methods for determining the Amount A allocation, which could involve the use of allocation keys or other reasonable approaches. Further, the transition period should also allow Groups and tax administrations to actually achieve “early” certainty on more robust allocation mechanics for the post-transition period. For this reason, the initial transition period should be lengthy to allow the first round of affected Groups and tax administrations sufficient opportunity to develop appropriate allocation mechanisms that are customized to each taxpayer’s business.

In addition, the transition concept should not be limited to the initial years following the adoption of Pillar One. Rather, there should be a comparable transition process for Groups that become in scope in later years, as these Groups and the affected tax administrations will face the same challenges developing appropriate allocation mechanisms.

The Consultation Draft provides limited information on the transitional period, and hence it is not possible to provide substantive feedback at this stage. However, we wish to stress that designing an effective transition approach is vital to the success of Amount A. We believe it will be essential to conduct a separate public consultation on transition issues once the requisite technical work is further along.

Role of MNE

We welcome the Consultation Draft’s recognition that the Lead Tax Administration will need to play a central role in the tax certainty framework, but we are concerned that this recognition does not extend to the involvement of the Coordinating Entity. Rather, the Consultation Draft appears to contemplate a passive role for the Group, which would be restricted to filing a documentation package and certainty request and thereafter passively responding to information requests.

We believe that the certainty process would be strengthened if the Coordinating Entity (and other Group entities, as appropriate) are more closely involved in the process. As with current ICAP, APA, and MAP cases, MNEs can fill a valuable role in the certainty process, both in terms of providing pertinent factual information

and suggestions with respect to realistic outcomes. Also, similar to APAs, the goal of the process is to find a consensus solution that the MNE can apply going forward, so the MNE should have more than a passive role in the process.

A review of a Group's application of Amount A requires specialized expertise outside the tax area, as recognized by the Consultation Draft's recommendation that an Expert Advisory Group be constituted. Some Affected Parties' tax administrations already employ personnel with such expertise, but may not have a sufficient number of qualified personnel to handle the volume of Amount A processes needed to support the number of in-scope MNEs that might wish to take part in the process. Other Affected Parties lack specialists who could perform this function.

Moreover, even where an adequate number of specialist tax examiners are available to review a Group's sourcing systems and other methodologies for applying Amount A, their ability to make sensible and workable recommendations would be hampered by their unfamiliarity with the Group's systems, data, and operating model. As such, if a certainty review includes a review of the Group's Amount A systems and internal control framework,⁴ Group personnel will need to be intimately involved in explaining to specialist tax examiners how the Group's systems collect, record, and process data, and in identifying what indicators can be reliably employed. A review that proceeds largely independent of Group involvement and relies on the Group only for information document request responses runs a high risk of proposing solutions that cannot be implemented, resulting in a certainty outcome that the Group cannot apply and wasting the time and resources of the Affected Parties involved in the process.

Because Group input is critical and needed to achieve a consensus agreement, Groups should be permitted to submit their views and analyses to the Affected Parties, the Review Panel, and the Determination Panel, and should be informed of all material aspects of the process, including advance notice and agendas of meetings and positions taken by the respective tax authorities. This is consistent with ICAP, APA, and MAP proceedings today, where MNEs play a valuable role in successfully resolving such cases.

Efficient Process Design

The Article 19 process described in the Related Issues Draft is an exemplary model of a process with fixed timeframes and default rules that will prevent deadlock and inappropriate delay. Carrying these laudable design choices over into the Amount A certainty processes would dramatically improve the workability of the tax certainty framework. The Consultation Draft's approach lacks fixed timeframes and provides opportunities for open-ended, iterative review and revision of Review Panel recommendations by Affected Parties, potentially thwarting tax certainty for relevant Periods.

Confidentiality

Addressing confidentiality issues is crucial to the successful implementation of Pillar One and should be the subject of a subsequent public consultation. The information necessary to determine the allocation of Amount

⁴ In many cases, a review of the Group's internal control framework should not be necessary at all. If a Group's internal control framework has been audited and certified by its external auditor, that certification should be accepted for Amount A purposes without the need for a separate review.

A is necessarily commercially sensitive, particularly in the case of Groups that compete against state-owned enterprises. While the Consultation Draft contains a few scattered references to confidentiality, its basic framework – namely, that the Lead Tax Administration will exchange sensitive Group data with all Affected Parties – seems to be predicated on the assumption that such exchanges can be accomplished in a manner where improper disclosure and impermissible use are not concerns. However, this ignores the realities of information exchange under current regimes, as well as the much greater risks associated with Amount A exchanges because of the large number of potential Affected Parties and the sensitive operational nature of some of the information that would be subject to exchange. To protect against these risks, it is imperative that the model rules permit the Lead Tax Administration (consistent with current exchange of information practice) to share information only when it has determined that the recipient can ensure the information will be kept confidential and used only for proper purposes, and that the information shared is directly relevant to the concerns of the requesting Affected Party. In addition, the model rules should expressly adopt a framework for enforcing confidentiality such as that under section 6103 of the U.S. Internal Revenue Code.

Dispute Resolution

The Consultation Draft envisions that some of the Affected Parties may opt to conduct a coordinated review of the application of Amount A to a Group in cases where the Group has not made a request for certainty, and the Consultation Draft provides that the Coordinating Entity would be permitted to request a Comprehensive Certainty Review in such a case. However, the framework for addressing cases that are not covered by a certainty request is insufficiently developed, and it is not clear that a Group would have access to mandatory and binding dispute resolution in all cases, as promised by the October Statement.

This is also true for cases in which a Group is removed from the certainty process, which could result from factors beyond the Group's control. The incidence of multiple taxation that would arise from the uncoordinated application of Amount A by all Affected Parties would be disastrous for a Group, and mechanisms would need to be developed to ensure that multiple taxation is avoided. To fulfill the October Statement's commitment to provide a dispute resolution mechanism as well as a dispute prevention mechanism, further technical work is needed in this area.



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