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Why S&S Approach as Amount B of Pillar One brings us nothing, at all

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Summary

On 19 February 2024 the Inclusive Framework on BEPS published its report on Amount B of Pillar One. The report adds to the discourse a standardised return-on-sales-oriented comparability analysis for the transfer pricing of low-risk distributors. The thing is called Simplified and Streamlined Approach (S&S Approach). Reading the report as it currently stands, the author wondered what the S&S Approach actually adds. What does it bring to the world? The answer is: nothing. Please read further below for some reasons why.

1 Introduction

On 19 February 2024, the OECD/G20 Inclusive Framework on BEPS (IF) published the announced report on Amount B of Pillar One.[2] Pillar One is the first of the two pillars (Pillar One, Pillar Two) to which the IF-countries have made a political commitment in 2021 to address the tax challenges arising from the digitalisation of the economy. Pillar One concerns the international political agreement on a formulary based profit tax base redistribution to market jurisdictions, the so-called Amount A, for the approximately one hundred largest multinationals worldwide. On 11 October 2023, the IF published the Multilateral Convention to Implement Amount A of Pillar One (MLC), a draft tax treaty to implement Amount A that is now awaiting to become a reality at some point in future. Pillar Two concerns the global 15% minimum tax system.

In addition to an Amount A, Pillar One also has an Amount B. The latter is a standardised return-on-sales-oriented comparability analysis for transfer pricing purposes for the pricing of so-called 'baseline wholesale marketing and distribution activities' of 'in-scope distributors' within the multinational group. For countries that choose to include such distributors with this type of distribution and marketing activities within their jurisdiction on this basis, the report provides for the application of the newly developed transfer-pricing approach to be either (i) mandatorily applicable to taxpayers, or (ii) made available to taxpayer as an elective mechanism. This is called the 'simplified and streamlined approach', the S&S Approach. The application of the S&S Approach does not have a minimum turnover threshold as is the case with the other components of the IF's two-pillar solution. This means that all multinational enterprises are affected by this, at least potentially that is. Jurisdictions opting in may apply the S&S Approach for tax years beginning on or after 1 January 2025. The OECD will publish and maintain on its website a list of jurisdictions applying the S&S Approach. The S&S approach is included as an Annex to Chapter

IV of the OECD Transfer Pricing Guidelines.[3] The guidance in the report will be updated in the coming period.

Reading the report as it currently stands, I wondered what the S&S Approach actually adds. What does the report bring to the world? The answer is: nothing. Please allow me to explain the reasons why in the paragraphs below.

2 Why S&S Approach as Amount B for Pillar One is of no use

2.1 Some general observations

Let us explore the report on Amount B and its backgrounds. The 52-page report follows its announcement by the IF in the Outcome Statement of 12 July 2023 and the subsequent public consultation that ran from 17 July 2023 to 1 September 2023.[4] These developments were subsequently followed up with the publication by the IF on 18 December 2023 of an update on the state of play and a revised timeline.[5] In addition to the report and a press release, the OECD published on its website a document entitled 'Reader's Guide for Pillar One – Amount B' which interested readers are referred to here.[6] The report gives some examples of the application of the newly developed system in an appendix (Appendix B – Illustrative examples). The interested reader is also referred to that.

The report states that the IF is currently working on an additional optional scoping rule, the so-called 'qualitative criterion', to identify eligible distributors and indicates that it expects to have completed the work on this by the end of March 2024. This scoping rule will also be included in the OECD Transfer Pricing Guidelines. India has made several reservations,[7] for example that an "appropriately designed qualitative criterion is critical to ensure that only baseline distributors are in scope of Amount B," so much so that "India expresses inability to support the Amount B work further if such a criterion is not incorporated as part of the scoping criteria in this report". India has also put in place reservations against "the overall design of the pricing methodology". The country, moreover, has included specific reservations in the report on a number of points.

A reference should be made here to footnote 3 in the introduction to the report.[8] The footnote states that: 'the content of this report, including any design elements, should be considered without prejudice to any future work on Amount B, such as on the interdependence of Amount B with the signing and entry into force of the MLC.' We should not pre-empt things and not assume, for example, that with the publication of this report, the signing and entry into force of the Multilateral Tax Treaty on Amount A would now be in the cards. Worthy of note, perhaps, is that the State Secretary for Finance of the Netherlands, the author's home country, in his letter of 24 October 2023 (No. 2023-0000235292) about the developments surrounding the two-pillar solution up to that point, wrote that a number of countries consider implementation of Amount A and Amount B to be part of the same agreement and that agreement with it must cover both parts.[9] This does not seem to have changed with the publication of the present report. The report provides a guarantee until the door, or so it seems.

The Outcome Statement writes about the now published document in terms of a report containing 'those elements' 'to ensure the appropriateness of the scope and pricing framework'.[10] The press release on the report on Amount B states that the S&S Approach that has now been presented is tailored to the needs of countries with low fiscal (implementation) capacity, so-called 'low-capacity jurisdictions', such as developing countries.[11] Notably, perhaps, in his letter to

parliament of 4 September 2023 (No. 2023-0000187366), the Netherlands' State Secretary for Finance also wrote that the measure is particularly beneficial for these types of countries.[12] According to the OECD press release at the time of publication of the report, several of these countries indicate that 30% to 70% of the transfer pricing disputes they face revolve around the pricing of the aforementioned marketing and distribution activities. In the aforementioned letter, the Dutch State Secretary for Finance wrote that the arm's length remuneration of marketing and sales activities is currently usually determined on the basis of a labour-intensive and subjective comparability analysis, which in practice gives rise to administrative burdens and discussions between taxpayers and countries and between countries. In the IF-report on Amount B[13] it can be read that discussions and resulting disputes sometimes revolve around the identification and selection of 'non-domestic comparables' (Q: Are Asian and European distributors and their profit margins comparable?) and/or the question of how to make an appropriate adjustment (comparability adjustment) for arm's length reasons.

The OECD's press release accompanying the publication of the report says that "[t]he approach set out in this report answers the call of low-capacity countries for what the African Tax Administration Forum (ATAF) has described as "vital" changes to the OECD Transfer Pricing Guidelines, providing what "could be a game changer for the African transfer pricing landscape".[14] "The changes to the OECD Transfer Pricing Guidelines agreed in this report will provide jurisdictions with the option of applying straightforward bright-line rules to these activities, allowing them to secure revenue and preserve valuable tax administration resources while providing additional certainty to multinational enterprises," the press release says.[15] Simple, legally certain, revenue raising for developing countries, that sounds wonderful, of course. Let's see how the rules work.

2.2 How the S&S Approach works

2.2.1 Countries are free to apply the S&S Approach

Countries are free to decide whether or not to apply the S&S Approach. The new transfer pricing approach is optional, countries are not obliged to implement the mechanism in their company tax rules. Countries that do not embrace the S&S Approach are also not obliged to conform to the results of the S&S Approach application in other countries, on both sides of the transaction, that will apply the new transfer pricing approach. In the report, IF countries express a conditional commitment – "subject to domestic legislations and administrative practices"[16] – to comply with the results of the S&S Approach where appropriate and to achieve single taxation under applicable tax treaties. This is the case if the relevant S&S Approach applying jurisdiction is a (as yet undefined) 'low-capacity jurisdiction'. The IF will publish a list of these types of jurisdictions by 31 March 2024 at the latest. The IF announces that it will be working on competent authority agreements that can serve to implement the aforementioned commitment in the tax treaty networks of the countries involved. India has indicated that it does not want to be bound by this commitment or by various other parts of the report, such as the points already mentioned about the scope rule and the overall design of the S&S Approach. On closer inspection, the ranks within the IF do not seem to be completely closed.

The jurisdictions that opt for the application of the S&S Approach can then choose to apply it: (i) make it mandatory for taxpayers (prescriptive), or; (ii) make it available to them as an elective regime, i.e., as a safe harbour. The idea behind the S&S Approach is to approximate the arm's-length remuneration for activities within the scope of the mechanism in a flat-rate manner for

simplicity reasons, while taking into account the principles of the OECD Transfer Pricing Guidelines. The S&S Approach is not intended to deviate from these principles. It is also not the intention to apply the S&S Approach outside the set frameworks. Nor is any precedent intended in that regard. Outside the scope of the S&S Approach, the regular OECD Transfer Pricing Guidelines apply. It seems that the S&S Approach is not intended to become eligible for countries and taxpayers as a readily available tool to run off with.

2.2.2 Scope of application S&S Approach (functional analysis)

The S&S Approach is somewhat limited and only applies to the pricing of ‘wholesale baseline marketing and distribution activities’ of ‘in-scope distributors’. This requires an ‘accurate delineation of the qualifying transaction’, the report says,[17] which requires a functional analysis (functions performed, assets used, risks assumed) that is customary in the transfer pricing domain. The S&S Approach focuses on marketing and distribution activities of (buy-sell) distribution companies, agents or commissionaires, where the related transaction is on the cost side (purchasing) and the distributor cs. concerned addresses unrelated parties in the sales market with regard to the involved products sold. The S&S Approach focuses on wholesale activities, in other words B2B activities. Transactions to consumers, B2C activities, retail activities that is, fall outside the scope of the S&S Approach. This is with the exception of so-called *de minimis* retail sales, which is the case when the retail sales in question do not exceed 20% of the total sales of the distributor concerned (by reference to a three-year weighted average). In that case, the S&S Approach may also be applied to those activities.

The S&S Approach requires that the economic characteristics of the related transaction(s) involved allow the transfer price to be reliably determined on the basis of a one-sided transfer pricing method, whereby the distributor cs. concerned is the tested party in the comparability analysis. The S&S Approach does not extend its scope of operation to distributors who are exposed to economically significant risks, who make unique and valuable contributions, for example in the context of intangible asset development and/or exploitation, and/or whose business operations are highly integrated with the other activities of the multinational company concerned. The distributor and its functions performed must therefore be segregable, low-risk, and therefore quantitatively moderately profitable; routine distribution activities that is. The sale of commodities, digital products and the performance of servicing activities fall outside the scope of the S&S Approach. Under certain circumstances, manufacturing activities fall within the scope of the S&S Approach. Non-distribution activities (i.e., research/development, procurement, financing, retail sales, etc.) may only be carried out if the transactions in question can be priced separately on the basis of the arm’s length principle under the operation of the regular OECD Transfer Pricing Guidelines.

The S&S Approach also requires that the operating expenses of the distributor in question fall within prescribed quantitative ranges, a ‘simplified mechanism’ called the ‘quantitative filter’: ‘[t]he tested party in the qualifying transaction must not incur annual operating expenses lower than 3% or greater than an upper bound of between 20% and 30% of the tested party’s annual net revenues’ (by reference to a three-year weighted average; countries can choose a point in the upper bound.[18] Outside these ranges, the pricing methodology might lose reliability in practice, because it might imply a different functional profile, according to the report.[19] At the same time, the report immediately indicates that ‘quantitative scoping filters are used as a simplification measure and do not provide any definitive indication of what functions are performed or the characterisation for distributors that fall out of scope in general’.[20] Furthermore, matters are spoken of in terms of ‘appropriate operating expenses’ and ‘appropriate net revenues’, which

requires an ‘accurate delineation’ of the transaction taking into account the principles in the OECD Transfer Pricing Guidelines.[21]

2.2.3 Applicable Transfer Pricing Method (TNMM)

The report prefers the so-called transactional-net-margin method (TNMM) as the most appropriate transfer pricing method for the application of the S&S Approach with reference to the ‘most appropriate method principle’.[22] Under the TNMM, the operating profit margin (earnings before interest and taxes; EBIT) on an affiliated transaction (or set of affiliated transactions) with the profit margin that would have been achieved in a comparable situation on a comparable transaction (or set of transactions) with a third party (benchmark). As usual in the transfer pricing domain, the application of the comparable-uncontrolled-price method (CUP) is preferable where the taxable persons concerned carry out transactions with third parties in addition to its internal transactions and this method can be reliably applied to price the internal transactions concerned on the basis of available data. At the same time, it may be noted at this point that the application of the CUP does not seem to be the most obvious in practice. This, because of the lack, in particular, of comparable transactions with third parties among the taxpayers involved. In addition, commodities, with respect to which internal CUPs are sometimes available to be made use of as a comparable, are excluded from the scope of application, which further reduces the relevance of the application of the CUP method under the S&S Approach.

2.2.4 Return on sales (pricing matrix)

As an indicator for determining the net profit indicator of the distributor in question in the context of the comparability analysis, the operation of the S&S Approach has been linked to the so-called ‘return on sales’ (ROS), the profit margin in relation to turnover (EBIT/turnover ratio). In the comparability analyses that are carried out in current practice to determine the arm’s length remuneration of group affiliates in some cases, the arm’s-length profit margins are usually derived from commercial databases, compiled from publicly available financial statements, on the basis of benchmarking search criteria and any further manual interventions.

It is at this point where the S&S Approach intervenes by not referring to a benchmark analysis focusing on any individual case, as is currently the case in practice, but to the results of a generalised comparability analysis along similar lines, including manual interventions, carried out by (or on behalf of) the authors of the IF report. The report states that on this basis a global (not geographically representative) dataset of companies with ‘baseline wholesale marketing and distribution activities’ has been developed and that the financial information provided by this exercise forms the basis, at least partially, for the approach to arm’s length remuneration, which is then reflected in a ‘pricing matrix’ (Table 5.1).[23]

The arm’s length remuneration thus approximated is presented in a so-called ‘pricing matrix’ as segments on the basis of the following factors: ‘net operating asset intensity’ (OAS), ‘operating expense intensity’ (OES) and ‘industry groupings’ (IG 1 (perishable foods, construction materials, etc.), 2 (IT hardware, animal feeds, jewellery, et cetera – as well as ‘components not listed in group 1 or 3’), 3 (medical machinery, agricultural vehicles, etc.). The report does not refer to any underlying logic that would underlie this classification. OAS is a net operating assets to net revenue ratio, OES is an operating expenses to net revenue ratio. This ultimately leads to 15 possible profit margins that range from 1.50% to 5.50%. An appendix, Appendix A – Relevant benchmarking search criteria, contains some further explanatory lines about the search criteria

used. For the rest, it is not possible to identify anything from the processes employed that have resulted into the accordingly observed percentages that can be verified to any extent.

2.2.5 Primary return on sales; three-step process

The pricing of baseline distribution functions in a concrete scenario, by both taxpayers and tax authorities, then follows a three-step process. Based on this, the so-called ‘primary return on sales’, the initial turnover-related profit margin, is derived from the pricing matrix. Step 1 concerns the classification of the distribution activities in question into one of the categories of industry groupings provided. The 3 industry groupings form 3 vertical columns in the matrix. Step 2 concerns the identification of the relevant ‘factor intensity classification’ of the distributor in question in one of the 5 classes A to E. These classes form 5 horizontal rows in the matrix and are linked to the OAS level and OES level. For the classification into classes A-C, a high (more than 45%), med/high (between 30 and 44.99%) and med/low (between 15 and 29.99%) OAS level is employed. For the classification into classes D and E, a low (less than 15%) OAS level is employed. For classification in class D or E, a low OAS level is then combined with the OES level (if low OES level, i.e. less than 10%, then class E; if non-low OES level, i.e. 10% or higher, than class D). If the relevant product sales can be classified under several categories, a weighted average will have to be calculated by reference to the profit margins in the respective accompanying cells provided. This is Step 3. The combined column/row application (3 columns, 5 rows, 15 cells) delivers the ‘primary return on sales’, the initial profit margin ranging from 1.50% to 5.50%. 0.5% may be added and subtracted from the result of the weighted average calculation (step 3) in order to create a range in which each point on this range then qualifies as acceptable for S&S Approach purposes.

2.2.6 Operating expense cross-check; four-step follow-up process

The ‘primary return on sales’ identified in this way is then subjected to a sanity check, the so-called ‘operating expense cross-check’. The report speaks of a ‘guardrail within which the primary return on sales net profit indicator is applied’.[24] If the initial profit margin falls outside a pre-defined operating expense cap-and-collar range (Table 5.2), the profit margin of the distributor in question will be adjusted for the purposes of application of the S&S Approach in order to bring it within the said range.

The application of the cross-check mechanism requires a four-step process. Step 1 concerns the determination of the equivalent return on operating expense equivalent to the initial profit margin determination. This is in fact a translation of the primary return on sales, the initial turnover-related profit margin, into a cost-related profit margin variant. Step 2 concerns the derivation of the applicable operating cap-and-collar range from Table 5.2. The applicable collar rate, the lower end of the range, is 10%. The applicable cap rate, the upper end of the range, is variable. The cap rates vary depending on the OAS level of the distributor concerned and are set at 70%, 60% and 40% at a high OAS level (Class A), medium OAS level (Class B and C) and low OAS level (Class D and E) respectively. This is the so-called ‘default cap rate’. For so-called (as yet undefined) ‘qualifying jurisdictions’, increased cap rates, so-called ‘alternative cap rates’, apply. These are determined using the same OAS levels and are set at 80%, 70% and 45% respectively. Step 3 concerns a comparison of the determined ‘equivalent return on operating expense’ of the distributor concerned from the first step with the stated ‘operating cap-and-collar range’ from the second step. Step 4 tells you what to do with the outcome of the comparison. If the equivalent return on operating expense falls within the range, the ‘primary return on sales’ does not need to be adjusted further. If

the equivalent return on operating expense exceeds the operating expense cap, the primary return on sales must be adjusted downwards to the level corresponding to an equivalent return on operating expense equal to the operating expense cap. If the equivalent return on operating expense below the operating expense collar, the primary return on sales must be adjusted upwards to the level corresponding to an equivalent return on operating expense equal to the operating expense collar.

On this basis, a renewed return on sales is established. I didn't see any mentioning of a definition of this notion in the report, such as perhaps a "modified" or perhaps a "secondary" return on sales, or something of that nature. The report leaves the rationale and bases for these approaches and percentages in limbo. India has explicitly indicated that it has great difficulty, an 'in-principal objection', with the cost-oriented cross-check mechanism.[25] This is because, rightly in my view, they do not see how cost levels can reflect value creation. I will not discuss the substantive merits, whether or not, of the three- and four-step mechanisms and further details. In the passing I heard that some countries think the percentages are too high and others too low.

2.2.7 Data availability mechanism; qualifying jurisdictions

For the so-called 'qualifying jurisdictions', a so-called 'data availability mechanism' then applies, on the basis of which the remuneration for the distribution function in question can be increased. This mechanism is intended to provide for cases where a distributor performs the activities to be priced in a jurisdiction for which no data is available or sufficiently available in the aforementioned global dataset and this jurisdiction is a 'qualifying jurisdiction'.[26] A footnote in the report[27] refers to some lines in the OECD Transfer Pricing Guidelines[28] about making transfer pricing adjustments for arm's length reasons due to local market characteristics and where local comparables cannot be reliably determined. In practice, the data on which to base 'comparables' is not always available in some developing countries.

The S&S Approach provides that in the case of distribution functions in such a qualifying jurisdiction, the return on sales, as determined in the manner set out above, is modified, i.e. increased. This, using the following formula: Adjusted return on sales = ROS_{TP} + (NRA_j x OAS_{TP}). The ROS_{TP} concerns the 'return on sales' in the hands of the distributor in question as determined in this manner. The NRA_j concerns the so-called 'net risk adjustment percentage', determined on the basis of the application of a table in the report (Table 5.3) that is linked to the so-called 'sovereign credit rating' of the relevant jurisdiction according to one of the well-known rating agencies. A BBB+ rating yields a net risk adjustment percentage of 0.0% and a CCC- rating or lower a percentage of 8.6%. The authors of the report found the inspiration for the determination of the percentage in the work of Professor Damodaran (footnote 39) without further citation of some sources. The OAS_{TP} by which this percentage is multiplied concerns the 'net operating asset intensity' of the distributor in question as set out above, which is capped at 85% for the purposes of the present data availability mechanism. Thus, for qualifying jurisdictions, under this mechanism, the EBIT/turnover ratio as shown by a generalized comparability analysis is increased by an amount equal to a percentage derived from a country's credit rating as multiplied by the assets-to-turnover ratio of the distribution company concerned. Here, too, the report leaves the rationale and bases for these percentages in limbo.

The result of the exercise is the 'adjusted return on sales', i.e. the approximate profit margin for transfer purposes of the aforementioned distribution functions of the distributors cs involved on a

turnover basis. The report indicates that '[i]n order to simplify compliance burdens associated with administering the simplified and streamlined approach' the analysis underlying the established ranges and percentages should be updated every 5 years. This is unless a significant change in market conditions requires an interim update. The financial data and other data points referred to in the report will be reviewed annually and adjusted where necessary. In short, periodic updates and black swan events on an ad-hoc basis. The OECD will also publish and maintain on its website a list of jurisdictions that qualify for the application of alternative cap rates and the data availability mechanism. The criteria on the basis of which countries will or will not qualify will be included in an update of the report.

2.2.8 Documentation requirements

There are some administrative aspects to the application of the S&S Approach. The report sets out the documentation obligations of taxpayers, in line with the transfer pricing documentation guidelines in the OECD Transfer Pricing Guidelines. In order to provide the tax authorities with the necessary information to be able to apply the S&S Approach, taxpayers must make such available through, for example, their local file or otherwise. This includes a sharing of information on, for example, internal financial reporting, the organizational/management structures, the allocation of revenues, costs, assets and liabilities, the consistencies of these, functional analyses, contracts, profit margin calculations and transfer pricing reconciliations. The key is for taxpayers to make the necessary information available, and where necessary over several years, so that the authorities can determine whether the scope rules have been complied with and whether the prescribed pricing system has been applied correctly. Taxpayers who wish to apply the S&S Approach for the first time, for example when the S&S Approach has been made available to them as an elective mechanism, must agree to commit themselves to it for a period of 3 years (subject to changes in facts or circumstances).

2.2.8 Avoidance of double taxation by mutual agreement

The report acknowledges that the application of the S&S Approach can give rise to economic double taxation. This may, for example occur, if (i) one jurisdiction, on one side of the transaction, applies the S&S Approach, while the other jurisdiction, on the other side of the transaction, does not, or if (ii) the jurisdictions involved apply the S&S Approach differently from each other. The report seeks to resolve matters by means of a corresponding transfer pricing adjustment and, where necessary through the best efforts obligations of countries under the mutual agreement procedure; MAP) and/or a competent authority agreement. Bilateral and multilateral advance pricing agreements (APAs) from before the S&S Approach entered into force continue to be valid.[29]

The report stipulates that if one of the jurisdictions concerned does not apply the S&S Approach, the other jurisdiction, i.e. the jurisdiction that does apply the S&S Approach, will determine its position in the context of the mutual agreement procedure on the basis of the application of the arm's length principle and the OECD Transfer Pricing Guidelines, without taking into account the S&S Approach. In that case, the S&S Approach is taken out of the equation and the S&S-Approach-applying jurisdiction then steps down where necessary to secure a single taxation. The report refers to some lines in the OECD Transfer Pricing Guidelines,[30] where it is noted in relation to safe harbours that jurisdictions 'should generally be prepared to consider modification of the safe-harbour outcome in individual cases under mutual agreement procedures to mitigate the risk of double taxation', i.e., for '[o]bviously, … if the jurisdiction in question refuses to consider double tax relief, the risk of double taxation would be unacceptably high and inconsistent with

double tax relief provisions of treaties'.[31] The report states its intention to amend the OECD Commentary on Article 25 of the OECD Model Convention, which regulates the mutual consultation procedure, accordingly on the occasion of a subsequent round of updates.[32] It is also stated that taxpayers cannot rely on the fact that the S&S Approach could be used to justify the arm's length nature of internal pricing in countries where this approach is not applied.[33]

In short, if and to the extent that the S&S Approach gives rise to double taxation, the jurisdiction applying the S&S Approach will withdraw. Any other outcome would be unacceptable and also inconsistent with any tax relief obligations under the double tax treaties, as the report observes in conjunction with the OECD Transfer Pricing Guidelines. This implies that the S&S Approach conflicts with the arm's length principle as soon as the S&S Approach's application gives rise to a different pricing than that applied under the arm's length principle pursuant to the applicable transfer pricing provision (in accordance with Article 9 of the OECD Model Convention) in the relevant tax treaty involved, i.e., without the application of the S&S Approach. This also implies that the S&S Approach, unless its outcome more or less coincidentally corresponds with that as applied under the arm's length principle pursuant to Article 9 of the tax treaty, can only have an effect in treaty situations if explicitly incorporated in the relevant tax treaty, for example in a protocol or in an instrument of public international law otherwise (e.g., a multilateral convention). The route of implementation of the S&S Approach via an administrative agreement between implementing institutions on the basis of a competent authority agreement, a solution proposed in the report is not enough to cater for such.[34] This is unless we were to allow institutions other than the judiciary to interpret treaty provisions, which would encounter fundamental objections of a constitutional nature. Worthy of note, perhaps, for illustrative purposes is the ruling of the Dutch Supreme Court of 6 January 2017 in which the court held a generic mutual agreement outcome between the competent authorities of the Netherlands and Germany on the distribution of taxing rights involving severance payments of cross-border workers null and void for being in contradict with the rule of law.[35] There is not much wording devoted in the report as to the constitutional foundations or the rule of law merits underlying the S&S Approach and its effectuation.

3 What does the S&S Approach bring to the world?

Reading the report as it stands, I wondered what the S&S Approach actually adds. What does the report bring us? What's in it for developing countries?

The answer is: nothing at all. Referring to the above, the S&S Approach does not bring administrative simplicity. On the contrary. It only adds transfer pricing hassles. Companies and tax authorities will have to carry out several transfer pricing analyses and calculations at the same time and then wait and see what the outcome will be in due course in any relevant jurisdiction. The S&S Approach does not bring legal certainty. The optionality and the lack of any result-oriented legal embedding makes the S&S Approach a giant with feet of clay.[36] No outcome is guaranteed, only controversy is. The S&S Approach does not secure any substantive tax revenues. Note that the S&S Approach is about routine activities, and hence, moderates amounts of profits, fixed, on a flat-rate basis and on esoteric and alchemical grounds. The S&S Approach equals mirrors and beads, which the aforementioned low-capacity jurisdictions will have to immediately surrender at the first counter-pressure from a jurisdiction on the other side of the transaction. A press release that tells us that the world will be a better place with such a newly devised transfer pricing gimmick, of course, will not change that.

To be honest, I find it rather staggering that this is all happening before our eyes and – with the

exception of India – not a single country within the IF context seems to have stood up to wonder aloud what we are actually doing here together. In the meantime, I saw that IF-member New Zealand has announced that it does not want to participate in the S&S Approach.[37] Moreover, I did not see an exception being made for 'low-capacity jurisdictions'. "The existing simplification measure for small foreign-owned wholesale distributors remains available and existing transfer pricing rules apply in all other cases," the New Zealand government says on its website.[38] In the passing I heard that various countries are now considering whether or not to embrace the S&S Approach. We will see.

4 Concluding remarks

It is becoming increasingly clear that, on some closer inspection, the two-pillar solution does not actually seem to be solving anything. We are seeing that the Pillar Two project has been turning into the anticipated whack-a-mole planning-and-anti-abuse-response fiesta,[39] while countries seek to mitigate any top-up tax implications via subsidy mechanisms.[40] At the same time, Pillar Two, it seems, stands at odds with tax conventions,[41] investment agreements,[42] human rights conventions,[43] and primary EU law (the latter for the jurisdictional blending concept being at odds with the very notion of the internal market without internal frontiers). We are awaiting some follow-up since the launch of the Multilateral Convention to Facilitate the Implementation of the Pillar Two Subject to Tax Rule, notably, regardless of the underlying merits of that instrument. The Multilateral Convention to Implement Amount A of Pillar One is awaiting follow-up, while the single most important country on which the success of that part of the Pillar One project hinges appears to have no intention of moving.

And now we also have the S&S Approach. If it really is the intention to secure some revenue for 'low-capacity jurisdictions' – who wouldn't want such a label? – via the company tax system, more or less simply, by means of a fixed transfer pricing remuneration for the performance of routine business activity, then it could of course also be agreed within the IF that these countries are allocated an x% profit margin, lay this down in a multilateral tax treaty and then actually ratify it. And then, we won't talk about it anymore. Then again, perhaps worthy of note, there is a huge debate in the Netherlands going on, today, on the question as to how to re-organize the Dutch capital income taxation system for individuals after its collapse since the Dutch Supreme Court, in 2021, held the flat-rate return mechanism in the Dutch income tax rules to infringe human rights conventions for its non-alignment with economic realities.[44] Any flat-rate arm's length remuneration, too, seems to diverge from economic realities. Perhaps a reorientation on rich-country budgets for development cooperation could be an alternative route to follow here. Be that as it may, back to company taxation, when it comes to taxing businesses, any of this would still concern some fiddling around in the margins.

When it comes to company tax reform, there are alternatives. For decades, international tax scholarship has been producing literature on how we could appropriately subject investment returns of multinational companies to business taxation. A wide range of suggestions for genuine and fundamental corporate tax reform worth exploring have already been put forward in literature, with the suggestions submitted ranging from supply-side oriented global (residual) profit-splitting systems to supply-side or demand-side global formulary systems, and extending even to destination-based cash flow taxes.[45] All merit consideration, while I have arrived at the idea of taxing groups on their economic profit at destination.[46] I don't think it's a coincidence that none of the findings in literature on company tax reform options have been devised along the lines of what we're seeing here today with the two-pillar solution. Perhaps someday we will witness a

moment of reflection in the international tax policy debate. We'll see.

[1] Maarten de Wilde is affiliated with Erasmus School of Law, Erasmus University Rotterdam, and PwC Rotterdam, the Netherlands. The paper is an English version of a forthcoming commentary on the developments involving Amount B in the Dutch tax weekly Nederlands Tijdschrift voor Fiscaal Recht. The English language version has been devised with the help of some AI-tooling. The manuscript has been drafted on 1 March 2024.

[2] OECD (2024), *Pillar One – Amount B: Inclusive Framework on BEPS*, OECD/G20 Base Erosion and Profit Shifting Project, OECD

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[3] OECD (2022), *OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2022*, OECD Publishing, Paris (OECD TPGL).

[4] OECD/G20 Base Erosion and Profit Shifting Project, Outcome Statement on the Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy, 11 July 2023, available at https://www.oecd.org/tax/beps/outcome-statement-on-the-two-pillar-solution-to-address-the-tax-challenges-arising-from-the-digitalisation-of-the-economy-july-2023.htm (Outcome Statement) , and OECD, Public Consultation Document, Pillar One – Amount B, 17 July 2023 –1 September 2023, available at https://www.oecd.org/tax/beps/oecd-invites-public-input-on-amount-b-under-pillar-one-relating-to-the-simplification-of-transfer-pricing-rules.htm.

[5] OECD/G20 Base Erosion and Profit Shifting Project, Update to Pillar One timeline by the OECD/G20 Inclusive Framework on BEPS, 18 December 2023, available at https://www.oecd.org/tax/oecd-g20-inclusive-framework-releases-new-information-on-key-aspects-of-the-two-pillar-solution.htm.

[6] OECD (2023), *Reader's Guide for Pillar One – Amount B: Inclusive Framework on BEPS,* OECD, Paris.

[7] See Amount B report, *supra note* 2, at 8 (footnotes 1, 4)

[8] *Ibidem*.

[9] The letter (in Dutch) is available at https://open.overheid.nl/documenten/2774df02-1f61-47f9-afe4-2a71aa2b28b6/file.

[10] See Outcome Statement, *supra note* 4.

[11] The press release is available at https://www.oecd.org/tax/beps/release-of-report-on-amount-b-relating-to-the-simplification-of-transfer-pricing-rules-and-conforming-changes-to-the-commentary-of-the-oecd-model-tax-convention.htm (Press Release).

[12] The letter (in Dutch) is available at

https://open.overheid.nl/documenten/a91a00f1-6e09-4ae2-a7be-e0cc57d14ae9/file.

[13] See Amount B report, *supra note* 2, at 14.

[14] Press Release, *supra note* 11.

[15] *Ibidem*.

[16] See Amount B report, *supra note* 2, at 6.

[17] See Amount B report, *supra note* 2, at 17.

[18] *Idem*, at 18.

[19] *Idem*, at 20.

[20] *Idem*, at 20 footnote 22).

[21] *Idem*, at 20 (footnote 24).

[22] *Idem*, Chapter 4, at 25.

[23] *Idem*, at 27.

[24] *Idem*, at 28.

[25] *Idem*, at 8 (footnote 9).

[26] *Idem*, at 30.

[27] *Idem*, at 30 (footnote 36).

[28] TPGL, *supra note* 3, at paragraph 1.167.

[29] *Idem*, at 37.

[30] *Idem*, at 15-16.

[31] TPGL, *supra note* 3, at paragraph 4.117 et seq., and paragtaph 4.131.

[32] Amount B report, *supra note* 2, at 7.

[33] *Idem* , at 37.

[34] *Idem*, at 37.

[35] Supreme Court of the Netherlands, 6 January 2017, ECLI:NL:HR:2017:6, available at rechtspraak.nl.

[36] See for a comparison Lauren Vella, Danish Mehboob, "U.S. Treasury Pushing for Mandatory Global Transfer Pricing Rules," Bloomberg Law, Feb. 21, 2024, available at news.bloombergtax.com.

[37] See the announcement of the country on https://www.ird.govt.nz/international-tax/business/transfer-pricing/simplification-measures.

[38] *Ibidem*.

[39] See for a comparison OECD (2023), Tax Challenges Arising from the Digitalisation of the Economy – Administrative Guidance on the Global Anti-Base Erosion Model Rules (Pillar Two), December 2023, OECD/G20 Inclusive Framework on BEPS, OECD, Paris available at https://www.oecd.org/tax/beps/administrative-guidance-global-anti-base-erosion-rules-pillar-two-december-2023.pdf, Maarten de Wilde, 'Is There a Leak in the OECD's Global Minimum Tax Proposals (GLOBE, Pillar Two)?', Kluwer International Tax Blog, March 1, 2021, available at https://kluwertaxblog.com/2021/03/01/is-there-a-leak-in-the-oecds-global-minimum-tax-proposals-globe-pillar-two/

[40] See, for instance, the draft decree that was released by Vietnam's Ministry of Planning and Investment, outlining an Investment Support Fund to counter the impacts of the Global Minimum Tax, available at https://www.vietnam-briefing.com/news/draft-global-minimum-tax-support-fund-unveiled.html/.

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[42] See, e.g., Blazej Kuzniacki, 'Pillar 2 and International Investment Agreements: 'QDMTT Payable' Seals An Internationally Wrongful Act', *Tax Notes International*, Vol. 112, No. 2, October 9, 2023, available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4598045

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[46] See M.F. de Wilde, *Sharing the Pie; Taxing Multinationals in a Global Market* (IBFD 2017), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2564181.

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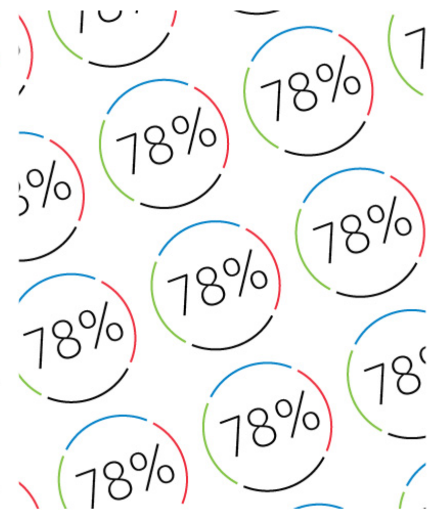

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