

OECD SECRETARY-GENERAL TAX REPORT TO G20 FINANCE MINISTERS AND CENTRAL BANK GOVERNORS

October 2019



G20 

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Please cite this publication as:

OECD (2019), *OECD Secretary-General Tax Report to G20 Finance Ministers and Central Bank Governors – October 2019*, OECD, Paris.

www.oecd.org/tax/oecd-secretary-general-tax-report-g20-finance-ministers-october-2019.pdf

Table of contents

Overview	5
1. Addressing the tax challenges of digitalisation.....	5
Background.....	5
Secretariat Proposal for a “Unified Approach” under Pillar One	6
Progress on Pillar Two.....	7
Preliminary findings of the Impact Assessment	8
Inclusivity	8
Next steps.....	8
2. Tax transparency	11
Tax transparency challenges arising from new technologies.....	12
Ensuring the level playing field through objective criteria.....	12
Annex 1: Secretariat Proposal for a “Unified Approach” under Pillar One.....	13
Annex 2: Application of the criteria to identify jurisdictions that have not satisfactorily implemented the tax transparency standards	26

Overview

G20 support for modernising the international tax rules has been instrumental over the past 10 years in ending bank secrecy, considerably improving tax co-operation, and strengthening the rules to counter base erosion and profit shifting (BEPS) by multinational companies.

However, further progress is needed to stabilise the international tax rules. The digitalisation of the economy has strained the existing rules to a point where they are exposed to a serious risk of fragmentation. A growing number of countries are taking unilateral measures or are departing from previously agreed standards. It is time to address these tensions and introduce some significant changes which will have to ensure that highly digitalised businesses can be taxed in states where users and consumers are located even though they are not physically present there. Fixing the international rules must be done in a way that is sustainable, removes existing tensions which go beyond digitalisation, and ensures both a proper elimination of double taxation and with better tax certainty. Good progress has been made by the OECD/G20 Inclusive Framework for BEPS (the OECD/G20 IF) with the adoption of a Programme of Work¹ in May 2019 which includes two main pillars: Pillar One, which provides a new allocation of taxing rights through a new nexus and profit allocation rules; and Pillar Two, which introduces measures to ensure a minimum level of tax. However, given persistent divergences of view on the three competing proposals under Pillar One, and in order to advance the discussions among members, the OECD Secretariat serving the OECD/G20 IF (the Secretariat) is proposing a “Unified Approach” under Pillar One. This Report includes the Secretariat proposal which, it is hoped, will be the basis for a negotiation that could result in a political agreement by mid-2020. This note also contains a report of the progress made on Pillar Two.

Finally, a brief update on the work on transparency is also included. This updates Finance Ministers on the jurisdictions that have not satisfactorily implemented the tax transparency standards.

1. Addressing the tax challenges of digitalisation

Background

In June 2019, I reported to you² that the constant efforts of the G20 over the past 10 years have changed the international tax environment, improving both its efficiency and fairness, with demonstrable progress on tax transparency and the implementation of the Base Erosion and Profit Shifting (BEPS) project. Your leadership on co-ordinated and multilateral approaches has delivered unprecedented results which have helped to repair the integrity and the fairness of the international tax system. **I also reported progress on the key outstanding issue of the BEPS**

¹ Programme of Work to Develop a Consensus Solution to the Tax Challenges Arising from the Digitalisation of the Economy, adopted on 28 May 2019. www.oecd.org/tax/beps/programme-of-work-to-develop-a-consensus-solution-to-the-tax-challenges-arising-from-the-digitalisation-of-the-economy.htm

² OECD Secretary-General Report To G20 Leaders, Osaka, Japan, June 2019: www.oecd.org/tax/oecd-secretary-general-tax-report-g20-finance-ministers-june-2019.pdf

Project: addressing the tax challenges of the digitalisation of the economy. I asked for your endorsement of the Programme of Work to deliver, by the end of 2020, a global solution to these challenges. These efforts, and your support, are necessary to stabilise the international tax system and to make it more robust in the face of the increasing globalisation and digitalisation of business activities. **In an environment marked by the threat of further unilateral measures to address these issues, it is essential to move forward now to construct the architecture of a global long-term solution through the G20/OECD IF.**

The Programme of Work that you endorsed in June 2019 consists of a **two-pillar approach**, aiming to provide for **new nexus and profit allocation rules on the one hand and a global anti-base erosion mechanism on the other**. However, as indicated in the Programme of Work, which the G20/ OECD IF has started implementing, the fact that three competing approaches were still being considered under Pillar One threatened the ability of the G20/ OECD IF to deliver a solution in time. In an effort to move swiftly to a “Unified Approach” under Pillar One, the Secretariat has developed a proposal aimed at facilitating consensus on common rules on nexus and profit allocation rules which would address the challenges of the digitalisation of the economy, while providing more certainty and stability in the international tax system for all countries and jurisdictions in the world.

Secretariat Proposal for a “Unified Approach” under Pillar One

The Secretariat’s proposed “Unified Approach” was recently presented to the members of the OECD/G20 IF at a meeting of its Task Force on the Digital Economy³ on 1 October. It has also been released for public comment by all interested stakeholders. It is attached to this Report for information (see Annex 1). The Secretariat’s proposal, which draws on the commonalities of the three alternatives originally proposed under Pillar One, has been guided by certain key principles: (i) seeking simplicity and administrability, (ii) keeping the current rules where they appear to function well enough and introducing changes beyond the arm’s length principle where necessary, (iii) providing for the elimination of double taxation, and (iv) increasing tax certainty to stabilise the rules through effective and binding dispute prevention and resolution mechanisms.

The Secretariat proposal suggests that a “Unified Approach” under Pillar One should focus on consumer-facing businesses, which would cover highly digitalised business models but would also go beyond, covering businesses interacting with final customers. It proposes a new nexus, distinct and separate from the existing concept of the permanent establishment, which would ensure a company is taxable in a territory where its sales exceed a certain threshold even if it is not physically present in that market. The scope of consumer-facing businesses, which would be limited to large companies, would also capture digitalised business models. The Secretariat proposal aims to reallocate to market jurisdictions a share of the deemed residual profit of MNEs falling within the scope (defined as exceeding a certain level of profitability)⁴ through a formula and based on consolidated financial accounts. It also proposes to allocate an appropriate fixed

³ 74 jurisdictions and 5 International Organisations attended the meeting of the Task Force of the Digital Economy on 1 October 2019.

⁴ It is expected that the relevant measure of profits would be derived from the group’s consolidated financial accounts.

return for distribution activities, to simplify and improve the administrability of the current rules. Finally, it recognises that the facts and circumstances approach under the existing arm's length principle rules may, in any particular case, trigger further taxing rights in the market/user jurisdictions but that, in any case, effective dispute prevention and binding dispute resolution between member jurisdictions would be needed to limit disputes and improve tax certainty.

In short, the "Unified Approach" provides a package which reallocates taxing rights to market jurisdictions in certain circumstances in exchange for improved tax certainty. The proposed approach recognises that the current rules do not fit the growing challenges of the digitalisation of the economy and proposes to address these challenges by establishing simplified/formulaic rules to allocate a portion of the profits of the more profitable companies, to countries and jurisdictions where customers are based, recognising that the interaction with consumers and users should be rewarded when companies have a sustained engagement in that market.

This proposal has been made by the Secretariat to facilitate a negotiation on the basis of the "Unified Approach", to allow the G20/OECD IF to make significant progress in the coming months so that a political agreement on Pillar One could be reached in the first half of 2020. The proposed "Unified Approach" remains a Secretariat proposal, even though it is hoped that members will advance their discussions on that basis. It is also worth noting that a number of questions are pending and need to be addressed, in particular as regards definitions, quanta, and the relationship of the new rules with existing rules. If this proposed "Unified Approach" becomes the basis for negotiation, members will be encouraged to promptly examine the key parameters and prepare what could be a political agreement between them.

Progress on Pillar Two

Parallel to Pillar One, good progress has also been made to develop the minimum tax proposal under Pillar Two known as the global anti-base erosion proposal (GloBE proposal). The Programme of Work articulated key design issues that need to be addressed, including the determination of the tax base, the extent to which the rules will permit blending of low- and high-tax income, and questions as to scope and thresholds for the application of the rules. The Programme of Work also directed the G20/OECD IF to consider issues around rule co-ordination as well as the interaction and compatibility of the GloBE proposal with international tax rules and obligations to ensure that the proposal avoids the risk of double taxation, minimises compliance and administration costs, and that the rules are targeted and proportionate.

Key parameters for Pillar Two are being examined in line with the Programme of Work and discussed at the technical level, with a public consultation foreseen in December 2019. **Some agreement has already been reached on the design of Pillar Two like the fact that it will operate as a top-up to an agreed fixed rate of tax that will be set once other key design elements of the proposal are finalised.** It is hoped that some of the main features of Pillar Two can be agreed by the next meeting of the G20/OECD IF in January 2020 while a political agreement on the architecture of Pillar Two would be expected in the first half of 2020 too.

Preliminary findings of the Impact Assessment

Work on the economic and tax revenue implications of the Pillar One and Pillar Two proposals has started but the final outcomes of this impact assessment will depend on the reform design and the behavioural responses of countries and multinational enterprises (MNEs) as well as refining data. This work is being informed by ongoing bilateral discussions with all IF members on country specific data and results.

At this point in time, preliminary findings suggest that the combined effect of Pillars One and Two would lead to a significant increase in global tax revenues as well as a redistribution of taxing rights to market jurisdictions. Pillar Two would yield significant increase of corporate income tax revenue globally. Pillar One involves a significant change to the way taxing rights are allocated among jurisdictions but it would also lead to a modest increase in tax revenues. MNEs in digital-oriented and intangible-intensive sectors would naturally be significantly impacted by both pillars. Overall, on average, low and middle-income economies would gain from Pillar One, experiencing a higher rate of increase in revenues than high-income economies even though, larger market jurisdictions will benefit more in absolute. Investment hubs, where the analysis suggests that levels of residual profit are high, would experience significant losses in tax base.

Both pillars would reduce the dispersion of effective tax rates and reduce the profit-shifting incentives of MNEs. Furthermore, given that the counterfactual to a consensus-based solution would be a proliferation of unco-ordinated and unilateral measures and an increase in tax disputes, the package would not adversely affect the investment environment, but would instead provide greater tax certainty.

Inclusivity

The current negotiation of solutions under Pillar One and Pillar Two includes all 134 members of the G20/OECD IF on an equal footing with a number of developing countries playing a particularly active role through the Steering Group of the OECD/G20 IF (with Georgia, Ivory Coast, Jamaica, Nigeria, Senegal being members of the Steering Group, along with G20 non-OECD countries like Argentina, Brazil, China (People's Republic of), India, Saudi Arabia or South Africa), in the Task Force on the Digital Economy or other working parties. However, to ensure the voices of lower capacity developing countries are effectively incorporated into this work, a number of actions have been undertaken to support them.

A series of regional outreach and consultation events has been planned with regional events scheduled to take place before the end of 2019 in Central and East Asia, Latin America and Africa. The Secretariat is also working to support the active participation of developing country members of the OECD/G20 IF work throughout the process through briefing sessions and bilateral dialogue with technical specialists on each of the proposed elements under discussion.

Next steps

I encourage you all to closely monitor this work and instruct your delegates of the G20/OECD IF to agree at a political level on the main elements of the proposal as soon as possible, noting that some fundamental decisions will require your personal input. The proposed "Unified Approach" is particularly ambitious and will require some both a high level of ambition as well as a politically pragmatic approach to make it happen. Combined with Pillar Two, it also has some important consequences on both businesses and countries' revenues.

In conclusion, I would like to underline the urgency of moving this agenda forward. While some jurisdictions may not be inclined to compromise, failure to move forward will seriously jeopardise the timely delivery of a consensus-based solution requested by the G20. The proposed “Unified Approach”, which has been presented to the full membership of the G20/OECD IF, seems to have enough support to be the basis for a negotiation which could result in an agreement with enough political support, by in the first half of 2020. This will not be possible without your personal support and involvement. I look forward to reporting further progress at your February meeting.

2. Tax transparency

Since our last meeting, the Global Forum on Transparency and Exchange of Information for Tax Purposes (Global Forum) has pursued its peer review work as regards the implementation of exchange of information on request. It has also developed a methodology to peer review the implementation of automatic exchange of information (AEOI). All this will be discussed and approved at the next meeting of the Global Forum, which will also **celebrate the 10th anniversary of the establishment of the Global Forum, on 26 November 2019 in Paris, France. I invite you all to join this public event which will be a unique opportunity to take stock of the extraordinary progress made in a relatively short time line.** As you know, this work has been a success story of the G20, which demonstrates that effective co-operation can change the world and improve trust in the tax system and in multilateralism.

As I reported in June 2019, beyond the formal progress in the form of the **4500 bilateral agreements signed and ratified (up by over 15% since 2018)** and the high number of **signatories to the Multilateral Convention on Mutual Assistance (130 to date)**, tax administrations worldwide are now collecting tax revenues from AEOI. **Close to 50 million bank accounts were exchanged by the end of September 2019 for a total value exceeding EUR 5 Trillion and already close to EUR 100 Billion of additional tax revenues have been identified.** This is in addition to **bank deposits in international financial centres (IFCs) having fallen by approximately 34% over the past ten years for a decline of USD 551 billion.** A large part of that decline is due to the onset of the automatic exchange of information, which accounts for about two thirds of that decrease. Specifically, **automatic exchange of information (AEOI) has led to a decline of 20% to 25% in the bank deposits in IFCs over the past decade.**

The fight for tax transparency should not overshadow our successes in the fight against BEPS. Changes are massive on that front too:

- **25 000 exchanges of previously secret tax rulings have taken place since 2016, which is 4 000 more since I last reported in June 2019.**
- **80 jurisdictions (up from 62 jurisdictions last year) have engaged in the exchange of Country-by-Country reports (CbCR) on the activities, income and assets of multinational enterprises,** which began in June 2018. CbCR provides tax administrations with access to extensive and consistent information on the largest foreign MNEs, which pose the greatest potential BEPS risk to their jurisdictions, given their size and potential revenues at stake.
- Preferential tax regimes allowed multinationals to avoid tax on their international activities, contributing to base erosion. **Since 2015, over 285 regimes have been reviewed and virtually all of the regimes that were identified as harmful have been amended or abolished.** Around the world, harmful regimes can no longer be used by countries to attract the tax base from other countries by targeting non-residents and foreign income only.
- With the Multilateral Instrument to implement BEPS, covering 89 jurisdictions and already ratified by 35 as of 30 September 2019, treaty shopping, which deprives countries of billions of euros in revenue, is also coming to an end. **At this stage, all treaty shopping hubs have signed the Multilateral Instrument and tax administrations are reporting that they can see meaningful behavioural changes among taxpayers.**

Tax transparency challenges arising from new technologies

In response to the tax compliance risks posed by **crypto-assets, e-money and other new financial products**, and exactly 5 years after the initial endorsement of the Common Reporting Standard by G20 leaders, **the OECD is now undertaking a comprehensive review of the CRS, ensuring that it continues to provide an effective global firewall against international tax evasion in an increasingly digital financial age.**

Alongside changes to the Common Reporting Standard, the OECD is also working with tax authorities to build strategies for ensuring compliance with tax obligations in respect of crypto assets, and to ensure they have the tools to address the risks of financial crime posed by such assets, such as through practical training and speedy access to data.

Equally, recognising the impact of **digital platforms on the growth of the sharing and gig economies**, the OECD is developing a standardised reporting and exchange framework for interested jurisdictions. This will allow tax administrations to better track income generated by those deriving income through the use of digital platforms in the sharing and gig economies and avoid unnecessary compliance costs stemming from the proliferation of different unilateral reporting rules.

Ensuring the level playing field through objective criteria

To ensure a level playing field, you have asked the OECD to regularly report on the jurisdictions which fail to comply with the tax transparency standards. In June 2019, eight jurisdictions had not satisfactorily implemented the tax transparency standards. I can now report that currently seven jurisdictions⁵ are failing to satisfactorily implement the tax transparency standards, which is one less compared to June 2019.⁶ **The Global Forum on Tax Transparency and Exchange of Information for Tax Purposes is working closely with all of these jurisdictions to provide whatever assistance and guidance is necessary to ensure a global level playing field.** Further details on the application of the objective criteria are included in Annex 2 to this report.

I will report to you on the progress made next year and identify any jurisdictions that still do not comply by the time of your next meeting.

⁵ Brunei Darussalam, Dominica, Montserrat, Niue, Sint Maarten, Trinidad and Tobago and Vanuatu.

⁶ Israel commenced exchanges in July 2019 and therefore now satisfactorily implements the tax transparency standards.

Annex 1: Secretariat Proposal for a “Unified Approach” under Pillar One

Introduction

1. The tax challenges of the digitalisation of the economy were identified as one of the main areas of focus of the Base Erosion and Profit Shifting (BEPS) Action Plan, leading to the 2015 BEPS Action 1 Report.⁷ Policy discussion on those challenges remains an important part of the international agenda.

2. Following a mandate by G20 Finance Ministers in March 2017, the Inclusive Framework, working through its Task Force on the Digital Economy (TFDE) delivered an Interim Report in March 2018: *Tax Challenges Arising from Digitalisation – Interim Report 2018* (the Interim Report).⁸

3. Conscious of the ambitious G20 time frame and the significance of the issue, the TFDE further intensified its work following the delivery of the Interim Report. Drawing on the analysis included in the Action 1 Report as well as the Interim Report, and informed by the discussions at the July 2018 and December 2018 meetings of the TFDE on a “without prejudice” basis, a number of proposals were made by delegates to the TFDE. These proposals, together with the recent discussions and comments from members of the OECD/G20 Inclusive Framework, lay the grounds for the Inclusive Framework to agree on the way forward to achieving a consensus-based solution in 2020.

4. In January 2019, the Inclusive Framework issued a short Policy Note, which grouped the proposals under consideration into two pillars.⁹ Pillar One, with which this document is concerned, focuses on the allocation of taxing rights and seeks to undertake a coherent and concurrent review of the profit allocation and nexus rules. Pillar One comprises the “user participation”, “marketing intangibles”, and “significant economic presence” proposals. The Policy Note stated that these proposals would entail solutions that go beyond the arm’s length principle. Pillar Two is concerned with the remaining BEPS issues.

5. As part of the continuing work, a public consultation document was released on 13 February 2019, which sought input from external stakeholders.¹⁰

6. On 28 May 2019, the Inclusive Framework adopted a Programme of Work to develop a consensus solution to the tax challenges raised by the digitalisation of the economy.¹¹ This was subsequently endorsed by G20 Finance Ministers at their meeting

⁷ OECD (2015), *Addressing the Tax Challenges of the Digital Economy*, Action 1 – 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.

⁸ OECD (2018), *Tax Challenges Arising from Digitalisation – Interim Report 2018*, Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.

⁹ *Addressing the Tax Challenges of the Digitalisation of the Economy – Policy Note*, as approved by the Inclusive Framework on BEPS on 23 January 2019, OECD 2019, accessible at www.oecd.org/tax/beps/policy-note-beps-inclusive-framework-addressing-tax-challenges-digitalisation.pdf

¹⁰ Public Consultation Document, *Addressing the Tax Challenges of the Digitalisation of the Economy*, 13 February – 6 March 2019.

¹¹ OECD (2019), *Programme of Work to Develop a Consensus Solution to the Tax Challenges Arising from the Digitalisation of the Economy*, OECD/G20 Inclusive Framework on BEPS, OECD, Paris.

in Fukuoka on 8-9 June 2019, and by G20 Leaders in Osaka on 28-29 June 2019. The Programme of Work is a critical step towards responding to the request from the G20 to find and agree a consensus solution by the end of 2020.

7. The Programme of Work highlighted the commonalities of the three proposals presented to the TFDE to facilitate a consensus solution on Pillar One. It also identified various technical issues that need to be addressed and allocated this work to different working parties. However, the Programme of Work emphasised the necessity to agree on the outline of the architecture of a unified approach by January 2020, given the goal of arriving at a consensus solution by the end of 2020. It also acknowledged that without bridging the gaps between the three proposals, it will not be possible to deliver such a solution, which may in turn encourage more jurisdictions to adopt unco-ordinated unilateral tax measures, including measures that tax gross revenues. Any such occurrence would undermine the relevance and sustainability of the international tax framework, and would damage global investment and growth.

8. As highlighted in the Programme of Work, the stakes are very high. In the balance are: the allocation of taxing rights between jurisdictions; fundamental features of the international tax system, such as the traditional notions of permanent establishment and the applicability of the arm's length principle; the future of multilateral tax co-operation; the prevention of aggressive unilateral measures; and the intense political pressure to tax highly digitalised MNEs.

9. In recent months, in light of the high stakes and the need for a clear direction, the Secretariat has undertaken extensive consultations to develop a "Unified Approach" which is outlined in this document. This document also aims to illustrate its application through an example.

A "Unified Approach" – the Secretariat's Proposal

10. The three alternatives set out in the Programme of Work under Pillar One have a number of significant commonalities:

- though there is some variation in how the proposals address the digitalisation issue, to the extent that highly digitalised businesses are able to operate remotely, and/or are highly profitable, all proposals would reallocate taxing rights in favour of the user/market jurisdiction;
- all the proposals envisage a new nexus rule that would not depend on physical presence in the user/market jurisdiction;
- they all go beyond the arm's length principle and depart from the separate entity principle; and
- they all search for simplicity, stabilisation of the tax system, and increased tax certainty in implementation.

11. There are nevertheless gaps between the proposals. As noted, the focus on digital businesses varies, with the user participation proposal making specific reference to such businesses and the marketing intangibles proposal operating more broadly and not referring explicitly to digital businesses.

12. The nature of the reallocation of taxing rights also differs between the proposals, with the marketing intangibles and user participation proposals reallocating a portion of non-routine profit to the user/market jurisdiction, and the significant economic presence proposal looking at all profits (routine and non-routine) as the starting point.

13. The Secretariat has sought to develop a possible new approach based on the commonalities between the three proposals, taking account of the ultimate aim of these proposals, the views expressed during consultations, as well as the need to deliver a solution that is as simple as possible.

Summary of the proposal

14. It is thus essential to design a solution that attracts support from all members of the Inclusive Framework. The Secretariat's proposal for a "Unified Approach" has been developed with this goal in mind.

15. That proposal is summarised here at a relatively general level, recognising that certain aspects still require further work. A number of implementation and administration questions also need to be addressed. However, the technical work of the Secretariat, as well as consultations with the membership, indicate that this is a viable option. It draws on the three alternatives under Pillar One and the ensuing public consultation process, and aims to identify the key features of a solution, which would include the following:

- **Scope.** The approach covers highly digital business models but goes wider – broadly focusing on consumer-facing businesses with further work to be carried out on scope and carve-outs. Extractive industries are assumed to be out of the scope.
- **New Nexus.** For businesses within the scope, it creates a new nexus, not dependent on physical presence but largely based on sales. The new nexus could have thresholds including country specific sales thresholds calibrated to ensure that jurisdictions with smaller economies can also benefit. It would be designed as a new self-standing treaty provision.
- **New Profit Allocation Rule going beyond the Arm's Length Principle.** It creates a new profit allocation rule applicable to taxpayers within the scope, and irrespective of whether they have an in-country marketing or distribution presence (permanent establishment or separate subsidiary) or sell via unrelated distributors. At the same time, the approach largely retains the current transfer pricing rules based on the arm's length principle but complements them with formula based solutions in areas where tensions in the current system are the highest.
- **Increased Tax Certainty delivered via a Three Tier Mechanism.** The approach increases tax certainty for taxpayers and tax administrations and consists of a three tier profit allocation mechanism, as follows:
 - Amount A – a share of deemed residual profit¹² allocated to market jurisdictions using a formulaic approach, i.e. the new taxing right;
 - Amount B – a fixed remuneration for baseline marketing and distribution functions that take place in the market jurisdiction; and
 - Amount C – binding and effective dispute prevention and resolution mechanisms relating to all elements of the proposal, including any

¹² The deemed residual profit used for Amount A would be the result of simplifying conventions agreed on a consensual basis. This means that it would only seek to approximate, without precisely quantifying, the amount of residual profit of a MNE group (see below para. 30 and 35).

additional profit where in-country functions exceed the baseline activity compensated under Amount B.

16. In a digital age, the allocation of taxing rights can no longer be exclusively circumscribed by reference to physical presence. The current rules dating back to the 1920s are no longer sufficient to ensure a fair allocation of taxing rights in an increasingly globalised world. It is also true that a number of the proposals that have already been made to address highly digitalised businesses fail to capture significant parts of the digitalised economy (such as digital services and certain high-tech businesses). The Secretariat's proposal is designed to respond to these challenges by creating a new taxing right. Therefore, and consistent with all the proposals that have been made, the Secretariat proposal includes a new nexus. From this follows the need to revise the rules on profit allocation as the traditional income allocation rules would today allocate zero profit to any nexus not based on physical presence, thus rendering changes to nexus pointless and invalidating the policy intent. That in turn requires a change to the nexus and profit allocation rules not just for situations where there is no physical presence, but also for those where there is. Otherwise, taxpayers could simply side-step the new rules by using alternative forms of an in-country presence (whether a local branch or related entity), making the new taxing right elective for taxpayers and creating an open invitation for tax planning.

17. The Secretariat's proposal is designed to address the tax challenges of the digitalisation of the economy and to grant new taxing rights to the countries where users of highly digitalised business models are located. However, the approach also recognises that the transfer pricing and profit allocation issues at stake are of broader relevance. It recognises that current transfer pricing rules, even in a post-BEPS environment, face challenges. While there seems to be adherence among Inclusive Framework members to the principle that routine transactions can normally be priced at arm's length, there are increasing doubts that the arm's length principle can be relied on to give an appropriate result in all cases (such as, for example, cases involving non-routine profits from intangibles). Moreover, there seems to be agreement that the arm's length principle is becoming an increasing source of complexity and that simplification would be desirable to contain the increasing administration and compliance costs of trying to apply it. Thus, an "administrable" solution is essential, especially for emerging and developing countries. And a simple system will lower the risks of disputes, which currently endanger the cohesion of the international tax system.

18. Against that background, the proposed "Unified Approach" would retain the current rules based on the arm's length principle in cases where they are widely regarded as working as intended, but would introduce formula-based solutions in situations where tensions have increased – notably because of the digitalisation of the economy. The following sections describe the key components of the "Unified Approach" in more detail, including a number of important pending questions.

Scope

19. The allocation of a new taxing right to market jurisdictions through new nexus and profit allocation rules would recognise that in today's globalised and increasingly digitalised economy a range of businesses can project themselves into the daily lives of consumers (including users),¹³ interact with their consumer base and create meaningful

¹³ The term "consumer" generally refers to individuals who acquire or use goods or services for personal purposes (i.e. outside the scope of a professional or business activity), while the term "customer" generally includes all recipients of a good or service (including business customers that are not end-users).

value without a traditional physical presence in the market. These features could be said to be relevant for any business, but they are most relevant for digital centric businesses which interact remotely with users, who may or may not be their primary customers, and other consumer-facing businesses for which customer engagement and interaction, data collection and exploitation, and marketing and branding is significant, and can more easily be carried out from a remote location. This would include highly digitalised businesses which interact remotely with users, who may or may not be their primary customers, as well as other businesses that market their products to consumers and may use digital technology to develop a consumer base.

20. This supports the idea that the proposed “Unified Approach” should be focused on large consumer-facing businesses, broadly defined, e.g. businesses that generate revenue from supplying consumer products or providing digital services that have a consumer-facing element. It would also suggest that some sectors (for example, extractive industries and commodities) would be carved-out. Further discussion should take place to articulate and clarify this scope, including consideration of how a consumer-facing business might be defined and how the concepts of consumer products or consumer sales would deal with the supply of goods and services through intermediaries, the supply of component products and the use of franchise arrangements. Further discussion should also take place to consider whether other sectors (e.g. financial services) should also be carved out, taking into account the tax policy rationale as well as other practicalities. Such discussion should also include consideration of size limitations, such as, for example, the €750 million revenue threshold used for country-by-country reporting requirements.

A new nexus rule for the taxpayers in the scope

21. Currently, in a jurisdiction a non-resident company is taxable on its business profits only if it has a permanent establishment there. That means having some form of physical presence. Digitalisation has strained the applicability of this rule as companies can increasingly do business with customers in a jurisdiction without having a physical presence there. This is particularly true of the remote sales of highly digitalised businesses, whose activities have called into question the relevance of the existing physical presence rules – not least in the minds of the public and politicians.

22. In an increasingly digitalised economy, and perhaps beyond today’s business models, it seems likely that large businesses will conduct more and more consumer-facing and/or user-facing activities from a remote location, with no or minimal physical presence in the market. The new nexus rule would address this issue by being applicable in all cases where a business has a sustained and significant involvement in the economy of a market jurisdiction, such as through consumer interaction and engagement, irrespective of its level of physical presence in that jurisdiction. The simplest way of operating the new rule would be to define a revenue threshold in the market (the amount of which could be adapted to the size of the market) as the primary indicator of a sustained and significant involvement in that jurisdiction. The revenue threshold would also take into account certain activities, such as online advertising services, which are directed at non-paying users in locations that are different from those in which the relevant revenues are booked. This new nexus would be introduced through a standalone rule – on top of the permanent establishment rule – to limit any unintended spill-over effect on other existing rules.

23. The intention is that a revenue threshold would not only create nexus for business models involving remote selling to consumers, but would also apply to groups that sell in a market through a distributor (whether a related or non-related local entity). This would be important to ensure neutrality between different business models, and capture all forms of remote involvement in the economy of a market jurisdiction.

New and revised profit allocation rules

24. Once it is determined that a country has a right to tax profits of a non-resident enterprise, the next question is how much profit the rules allocate to that jurisdiction. This matter is currently answered by Article 7 (Business Profits) of both the OECD and United Nations Model Tax Conventions.

25. In the case of a resident enterprise transacting with its own affiliates, countries have taxing rights over the profits of that enterprise in accordance with Article 9 (Associate Enterprises).

26. While Articles 7 and 9 are a common feature of substantially all tax treaties, there is greater variation in the terms of Article 7. But most importantly, a large proportion of tax disputes for large MNE groups are about the interpretation and practical application of those articles, and this is particularly true for marketing and distribution activities.

27. As noted, given that the new taxing right would create a nexus for an MNE group even in the absence of a physical presence, it would be impossible to use the existing rules to allocate profit to this new nexus in cases where no functions are performed, no assets are used, and no risks are assumed in the market jurisdictions. Therefore, new profit allocation rules are required for Amount A.

28. As recognised in the Policy Note issued by the Inclusive Framework in January 2019, the new profit allocation rules would go beyond the arm's length principle and beyond the limitations on taxing rights determined by reference to a physical presence, two principles generally accepted as cornerstones of the current rules. At the same time, while a number of criticisms of the arm's length principle have been voiced, there is a recognition that the current rules work reasonably well for most routine transactions. Therefore, the new rules would allow for the taxation at an appropriate level of business activities in market jurisdictions, while retaining transfer pricing rules where they work relatively well in that market jurisdiction.

29. The new rules, taken together with existing transfer pricing rules, will need to deliver the agreed quantum of profit to market jurisdictions and do so in a way that is simple, avoids double taxation, and significantly improves tax certainty relative to the current position. It is also important that the new rules are reconciled with existing rules. That is, the new rules should not create distortions and should be effectively applicable to both profits and losses.

30. Against that background, the "Unified Approach" proposes the following three tier mechanism:

Amount A – A new taxing right for market jurisdictions over a portion of within the scope MNE groups' deemed residual profit. This could potentially be calculated on a business line basis. In broad terms, this deemed residual profit would be the profit that remains after allocating what would be regarded as a deemed routine profit on activities to the countries where the activities are performed. This would be determined by simplifying conventions, and require the determination of the level of the deemed routine profit and also a decision on the proportion of the deemed residual profit that should go to the market, which in turn would be allocated to particular markets meeting the new nexus rule through a formula based on sales. Percentages remain to be determined and would be part of the consensus-based agreement among Inclusive Framework members.

Amount B – Activities in market jurisdictions, and in particular distribution functions, would remain taxable according to existing rules (e.g. transfer pricing under the arm's length principle and permanent establishment allocation under

Article 7). However, given the large number of tax disputes related to distribution functions, the possibility of using fixed remunerations would be explored, reflecting an assumed baseline activity. Appropriate and negotiated fixed returns could provide certainty to both taxpayers and tax administrations, and reduce the dissatisfaction with the current transfer pricing rules.

Amount C – Any dispute between the market jurisdiction and the taxpayer over any element of the proposal should be subject to legally binding and effective dispute prevention and resolution mechanisms. This would include those cases where there are more functions in the market jurisdiction than have been accounted for by reference to the local entity’s assumed baseline activity (which is subject to the fixed return in B above), and that jurisdiction seeks to tax an additional profit on those extra functions in accordance with the existing transfer pricing rules.

31. There is a more detailed discussion of the proposed approach to profit allocation in the Appendix to this document.

Pending key questions

32. A number of the areas in which further work would be required are already covered by the Programme of Work. These include work on the possible use of business line or regional segmentation, issues and options in connection with the treatment of losses, and the challenges associated with the determination of the location of sales. Some of this work is already underway.

Differentiation for business models

33. It is recognised that some jurisdictions wish to explore the possibility of applying mechanisms to reflect some degree of potential digital differentiation, or some kind of weighting in the amount of profit that would be re-allocated to market jurisdictions, whether under Amount A or by adapting the approach to Amounts B and C. The merits and viability of any such approach (including possible options to deliver this result) would therefore have to be explored.

Definitions and quanta

34. The proposal raises certain additional issues on which technical work would be required, such as the definition of activities under Amount B or possible variations in the design of Amount A.

35. Similarly, agreeing multilaterally on the scale or amount of profits reallocated to market jurisdictions (in particular Amount A) will be an essential aspect of the “Unified Approach”. The amount of profits to be reallocated would be determined by simplifying conventions and will be informed by an impact assessment of the “Unified Approach”. However, the choice of this amount will ultimately be the result of a political agreement that needs to be acceptable to all members of the Inclusive Framework, small and large, developed and developing.

Elimination of double taxation

36. Because the existing domestic and treaty provisions relieving double taxation apply to multinational enterprises on an individual entity and individual country basis, the implementation of the proposed approach would require the identification of the member(s) of an MNE group that should be treated as owning the taxable profit in such market jurisdictions under Amount A (e.g. entity(ies) with high profitability, entity(ies) owning certain intellectual property (IP)). In particular, it will be important to explore to what extent identifying the relevant taxpayers and the relevant profit to be reallocated

would allow existing mechanisms for eliminating double taxation to continue to operate effectively. This would involve how domestic and treaties rules to relieve double taxation could operate under the “unified approach”.

37. In addition, approaches to address any risk of double counting or duplications between the three possible types of taxable profit (Amounts A, B and C) that may be allocated to a market jurisdiction would need to be considered, in particular interactions between the new taxing right under Amount A and current profit allocation rules. Similarly, specific rules would need to be considered for the treatment of losses under Amount A (e.g. claw-back or “earn out” mechanism).

Other implementation issues

38. An important objective in the implementation of the “Unified Approach” would be to strike a balance between keeping the compliance and administrative burdens as low as possible, while ensuring that taxpayers fulfil their new obligations.

39. Where the tax liability for Amount A is assigned to an entity that is not a resident of the taxing jurisdiction, enforcement and collection could be more complex. It is worth exploring whether a withholding tax would be an appropriate mechanism for the collection of the designated Amount A. However, if countries choose to use it (and as an administrative mechanism to simplify and assure the collection of an underlying taxing right, it would be a matter for domestic law) it would be necessary to agree the features of the system of withholding that jurisdictions could commit to apply.

40. Any proposal seeking an allocation of taxing rights over a portion of a non-resident enterprise’s business profits in the absence of physical presence, and computed other than in accordance with the arm’s length principle, would require changes to existing tax treaties. Different approaches could be envisaged to streamline the implementation of these changes and these options would need to be further assessed as part of the Programme of Work. More fundamentally, however, the re-allocation of taxing rights raises important political considerations. A crucial one is that these changes would need to be implemented simultaneously by all jurisdictions, to ensure a level playing field.

Illustration

Facts

41. The facts are as follows:

- Group X is an MNE group that provides streaming services. It has no other business lines. The group is highly profitable, earning non-routine profits, significantly above both the market average and those of its competitors.
- P Co (resident in Country 1) is the parent company of Group X. P Co owns all the intangible assets exploited in the group’s streaming services business. Hence, P Co is entitled to all the non-routine profit earned by Group X.
- Q Co, a subsidiary of P Co, resident in Country 2, is responsible for marketing and distributing Group X’s streaming services.
- Q Co sells streaming services directly to customers in Country 2. Q Co has also recently started selling streaming services remotely to customers in Country 3, where it does not have any form of taxable presence under current rules.

Application of the “Unified Approach” where a group has a taxable presence in the market jurisdiction (country 2)

42. In Country 2, Group X already has a taxable presence in the form of Q Co. This subsidiary is already contracting with and making sales to local customers.

43. Under the new taxing right (Amount A), it will be necessary to determine whether Group X has a new non-physical nexus in Country 2. For the purpose of this example, assume that Q Co makes sufficient sales in Country 2 to meet the revenue threshold. This would give Country 2 the right to tax a portion of the deemed non-routine profits of Group X (Amount A). Country 2 may tax that income directly from the entity that is treated as owning the deemed non-routine profit (in this example, P Co), with the possibility of Q Co held jointly liable for the tax due to facilitate administration. Relief from double taxation would be provided once P Co claims a foreign tax credit or an exemption in Country 1.

44. Q Co would be the taxpayer for the only applicable fixed return for baseline marketing and distribution activities (Amount B). Transfer pricing adjustments would be made to transactions between P Co and Q Co to eliminate double taxation.

45. Finally, if Country 2 considers that Q Co should have additional profits taxed under the arm’s length principle because its activities go beyond the baseline activity assumed in the fixed return arrangement for marketing and distribution activities (Amount C), Country 2 would be subject to robust measures to resolve disputes and prevent double taxation.

Application of the “Unified Approach” where a group does not have a taxable presence in the market jurisdiction (country 3)

46. In Country 3, Group X does not have a taxable presence under existing rules. However, Q Co is making remote sales in the country.

47. Under the new taxing right (Amount A), it will be necessary to determine whether Group X has a non-physical nexus in that jurisdiction. For the purpose of this example, assume that Group X makes sufficient sales in Country 3 to meet the revenue threshold.

48. This would give Country 3 the right to tax a portion of the deemed non-routine profits of Group X (Amount A). Country 3 may tax that income directly from the entity that is treated as owning the non-routine profit (i.e. P Co), with P Co being held to have a taxable presence in Country 3 under the new nexus rules.

49. As, under current rules, Group X does not have an in-country presence in Country 3 (branch or subsidiary), Amount B would not apply.

Appendix – Detailed proposal on profit allocation

50. The way to address profit allocation under the proposed “Unified Approach” described in outline earlier in this paper proposes three possible types of taxable profit that may, according to the circumstances in any particular case, be allocated to a market jurisdiction (which, in some instances, is the location of the user). The three types of profit are described further below. The new taxing right (through the profit that is referred to here as Amount A) would generally increase the amount of business profit allocated to market jurisdictions, including in the absence of physical presence. Importantly, the second and third type of profit (Amounts B and C) would apply only by reference to the presence of a traditional nexus in the market jurisdiction (a subsidiary or permanent establishment), and not in the case of a taxable presence resulting from the application of the new non-physical nexus rule (which would give rise to Amount A). A strong emphasis on dispute prevention and resolution is integral to each of the three types of profit that make up the proposed new profit allocation rules.

- **Amount A**

51. The first type of profit, Amount A, would reallocate a portion of the deemed residual profit of a multinational business (on a group or business line basis) to market jurisdictions irrespective of the location and/or residence of that business, consistent with the creation of a new nexus unconstrained by physical presence requirements. The deemed residual profit would represent the profit that remains after designating a deemed routine profit on the activities of the group or business line. This reallocation would specifically address the concerns raised by the remote and non-physical participation of some businesses in the economy of a market jurisdiction, and the question of how taxing rights on income generated from cross-border activities in the digital age are allocated. Similar to existing profit allocation rules, it would have effective application to both profits and losses, but specific rules may be considered for the treatment of losses (e.g. claw-back or “earn out” mechanism).

52. In broad terms, this approach would replicate features of both the residual profit split (RPS) method (by introducing a threshold based on profitability to exclude the remuneration of routine activities) and the fractional apportionment method (by relying on formula-based calculations). This combination presents two main advantages that contribute to the practicability of the proposal. First, it would permit the isolation of the deemed non-routine profits earned by a business. This is important because, by introducing a threshold based on profitability and targeting deemed non-routine profit, the proposed method is designed to materially limit the disruption of the conventional transfer pricing that is applied to routine activities. This would reduce the practical complexity of the proposal and also facilitate the goal of reaching consensus among the members of the Inclusive Framework (on the basis that no jurisdiction would be required to give up taxing rights over income generated by routine business activity physically located within its jurisdiction). Second, the use of simplified conventions would facilitate the administration of the new profit allocation approach alongside the current transfer pricing rules and reduce the scope for disputes – a feature contemplated by all Pillar One proposals.

53. The starting point for the determination of Amount A would be the identification of the MNE group’s profits. The relevant measure of profits could be derived from the

consolidated financial statements¹⁴ under the accounting standards of the headquarters jurisdiction prepared in accordance with the Generally Accepted Accounting Principles (GAAP) or the International Financial Reporting Standards (IFRS). The advantages of such an approach are that consolidated financial statements are (1) normally readily available and (2) not easily manipulated. To better approximate a proxy of residual profit, further consideration will need to be given to the appropriate measure of profits and also to potential standardised adjustments to the reported profit (as *per* the consolidated financial accounts). In addition, the fact that the profitability of an MNE group can vary substantially across business lines, regions or markets suggests that the relevant measure of profits may need to be determined on a business line and/or regional/ market basis. Otherwise, in the case of a business that combines a low-margin retail business line with a high-margin cloud-computing business line, distortions would arise that could benefit jurisdictions where the retail sales are concentrated, at the expense of jurisdictions where cloud-computing sales occur. This would also reduce the incentives the new taxing right may create for businesses to restructure. While this could create challenges, some assistance could be available from the fact that existing financial accounting reporting standards¹⁵ generally require publicly listed companies to disclose certain financial information by operating segments, which are typically based on business line and/or region, though this would clearly need further consideration. The task of determining the required data and documentation under the proposed approach would form part of the overall package of work.

54. The second step in calculating Amount A would seek to approximate the remuneration of the routine activities based on an agreed level of profitability. In broad terms, these are profits which, by analogy to the residual profit split method, would be regarded as rewarding routine functions. They are accordingly excluded from the calculation of the pool of profits from which the allocation to market jurisdictions would be made. The level of profitability deemed to represent such “routine” profits could be determined using a variety of approaches, but a simplified approach would be to agree a fixed percentage(s), possibly with variances by industry.

55. This simplified approach may be illustrated by an example. Assume that the proportion of profits to revenues (i.e. profit margin), derived from the consolidated financial statements as suggested above, is $z\%$. A portion of that percentage may be regarded as representing routine profits. If that portion is $x\%$, then $x\%$ would be ignored for the purposes of the calculation of the profits reallocated to market jurisdictions, with only the excess ($z\%-x\%$) being the subject of further consideration. In the discussion below, that excess is assumed to be $y\%$.

56. The completion of this step would not be intended to disturb the actual allocation of the remuneration derived from actual routine activities under the current transfer pricing framework. Instead, the purpose of the simplifying conventions would be merely to simplify the calculation of the deemed non-routine profit subject to the new taxing right.

57. Once profits in excess of the stipulated level of profitability are deemed to be the group’s non-routine profits, it is then necessary to determine the split of those deemed non-routine profits between the portion that is attributable to the market jurisdiction and the portion that is attributable to other factors such as trade intangibles, capital and risk, etc. This is important as non-routine profit generated by MNE groups

¹⁴ For a definition of the term “*consolidated financial statements*” see OECD (2015), Transfer Pricing Documentation and Country-by-Country Reporting, Action 13 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, p. 40.

¹⁵ For instance, IFRS and the US GAAP.

is attributable to many activities including those not targeted by the new taxing right. For example, a social media business may generate non-routine profit from its customers' data and valuable brand, but also from its innovative algorithms and software.

58. Given the practical difficulties of using conventional transfer pricing rules for this step, the proposed approach assumes that a share of the deemed non-routine profit attributable to the market jurisdiction would be determined in accordance with a simplifying convention, such as non-routine profit multiplied by an internationally-agreed fixed percentage, though it is possible that different percentages might be applied to different industries or business lines.

59. Returning to the example above, if the profit margin is $z\%$ from which $x\%$ is deducted on the basis that it represents the deemed routine profits, then the balance, assumed to be $y\%$, would be regarded as representing the group's deemed non-routine or residual profits. Under this third step, the amount of the non-routine profits – the $y\%$ – would then need to be allocated between the profits attributable to market jurisdictions (assumed here to be $w\%$) and the profits attributable to other factors such as trade intangibles (assumed here to be $v\%$). Again, a crucial aspect of the “Unified Approach” would be to determine and agree the method through which $w\%$ is determined, and whether this percentage should vary by industry.

60. The final step of the proposed approach would be to allocate the relevant portion of the deemed non-routine profit ($w\%$ in the above example) among the eligible market jurisdictions. This allocation should be based on a previously agreed allocation key, using variables such as sales. The selected variables would seek to approximate the appropriate profit due to the new taxing right.

61. An important aspect of this approach would be to determine the level of profitability to be taken as representing “routine” profits and also determine the portion or percentage of the deemed non-routine profit that should go to the market jurisdictions, through an allocation key based on sales. The level of profitability and the split of the non-routine profits could be determined using a variety of approaches, but, as illustrated in the discussion above, a simplified approach could be to agree on a formula through the application of fixed percentages, possibly with variances by industry.

- **Amount B**

62. The second type of profit would seek to establish a fixed return (or fixed returns, varying by industry or region) for certain “baseline” or routine marketing and distribution activities taking place in a market jurisdiction. The fixed return under Amount B would seek to reduce disputes in this area, where tensions are important as a result of applying the transfer pricing rules. The intention would be to benefit taxpayers and tax administrations, as it would reduce the risk of double taxation as well as the substantial compliance costs arising from the aggressive enforcement of current transfer pricing rules.

63. Whilst the distinction between marketing and distribution activities and others performed by an MNE group will, in most cases, be clear, there will be some borderline issues. Therefore, a clear definition of the activities that qualify for the fixed return would be required. The quantum of the fixed return could be determined in a variety of ways: it could be (1) a single fixed percentage; (2) a fixed percentage that varied by industry and/or region; or (3) some other agreed method.

- **Amount C**

64. Taxpayers and tax administrations would retain the ability to argue that the marketing and distribution activities taking place in the market jurisdiction go beyond the baseline level of functionality and therefore warrant a profit in excess of the fixed return contemplated under Amount B, or that the MNE group or company perform other business activities in the jurisdiction unrelated to marketing and distribution. In either case an additional profit – Amount C – would be due where this is supported by the application of the arm’s length principle, though this would require robust measures to resolve disputes and prevent double taxation. In this context (as well as in relation to any element of the proposal where a tax dispute arises in the market jurisdiction), it would be essential to consider existing and possible new approaches to dispute prevention and resolution, including mandatory and effective dispute prevention and resolution mechanisms to ensure the elimination of protracted disputes and double taxation.

65. In relation to Amount C, it would also be important to ensure that the profit under Amount A could not (whether in whole or part) be duplicated in the market jurisdiction, for example based on an argument that some or all of the profit under Amount A is also in some way referable to the functional activity in the market jurisdiction which is rewarded by Amount C. Further work on certain aspects of the detailed interaction of Amounts A and C would therefore be warranted.

Annex 2: Application of the criteria to identify jurisdictions that have not satisfactorily implemented the tax transparency standards

The identification criteria cover all members of the Global Forum on Transparency and Exchange of Information for Tax Purposes (the Global Forum), except developing countries without financial centres, as well as non-member jurisdictions that are identified by the Global Forum as relevant for the purposes of its work.

In order for a jurisdiction to be considered to comply with respect to international tax transparency, it would need to meet the benchmarks of **at least two of the three below-mentioned criteria**.

1. **The exchange of information on request (the EOIR standard):** a “Largely Compliant” overall rating, taking into account the Global Forum’s second round of reviews on an ongoing basis and provided jurisdictions (other than those that received a provisional rating in the first round) have had an opportunity to respond to any downgrades in rating through a supplementary report;
2. **The automatic exchange of information (the AEOI standard):**
 - a) All necessary legislation is in place and exchanges commenced by the end of 2018; and
 - b) Agreements are activated with substantially all interested appropriate partners by the end of 2019; and
3. Having the **Convention on Mutual Administrative Assistance in Tax Matters in force** or having a sufficiently broad exchange network of bilateral agreements in force permitting both EOIR and AEOI.

However, a jurisdiction will be considered as failing to comply notwithstanding that it may have met the benchmarks of two of the three criteria if:

- a) it is determined to be “non-compliant” overall for its implementation of the EOIR standard; or
- b) it has not met the AEOI benchmark set out above.

Criterion 1: Exchange of Information on Request (EOIR)

Exchange of information on request has grown in importance as co-operation in tax matters has spread more widely. The level of compliance with the EOIR standard is high: today, **out of 54 Global Forum members that have been reviewed in the second round of reviews, over 85% are rated at least “Largely Compliant” with the EOIR standard overall.**

Some Global Forum members that are developing countries without a financial centre have received a “Non-Compliant” or “Partially Compliant” overall rating in Round 2 but they are excluded from the scope of this exercise.

Of the jurisdictions that are within the scope of the listing exercise, two jurisdictions¹⁶ do not satisfactorily implement the EOIR Standard and fail to meet the EOIR criterion.

¹⁶ Trinidad and Tobago and Vanuatu.

In addition, 11 jurisdictions are otherwise “partially compliant” with the EOIR standard or have been provisionally rated “Largely Compliant”. The majority of these are currently being reviewed by the Global Forum and the most of their reviews are expected to be finalised by the end of 2019.

Criterion 2: Automatic Exchange of Information (AEOI)

In total, 100 jurisdictions committed to implement the AEOI Standard by 2018. Out of these, **seven jurisdictions are currently failing the criterion on AEOI with its two sub-criteria.**

Sub-criterion a): legislation is in place and exchanges commenced by the end of 2018

In June 2019, eight jurisdictions were identified as not having met this sub-criterion. Since the last report, Israel commenced automatic exchanges and now meets this sub-criterion.

In total, 93 of the 100 jurisdictions that committed to commence exchanges by 2018 have therefore now exchanged information. **Seven jurisdictions have yet to commence exchanges** (Brunei Darussalam, Dominica, Montserrat, Niue, Sint Maarten, Trinidad and Tobago and Vanuatu).

It is worth noting that Niue, Montserrat and Vanuatu have now completed all of the necessary legal and technical steps and may therefore commence exchanges shortly.

Sub-criterion b): Agreements activated with substantially all interested appropriate partners by the end of 2019

Part of the commitment to the AEOI Standard is to exchange information with all interested appropriate partners. Interested appropriate partners’ are defined as jurisdictions that are interested in receiving information from another jurisdiction and that meet the expected standards in relation to confidentiality and data safeguards. **To date, no gaps in the exchange networks in place have been identified, thanks to the Global Forum review process.**

A jurisdiction can trigger the review process when it is concerned about delays by potential partner jurisdictions in putting in place of an exchange relationship. The review is to establish whether an agreement should be put in place and therefore whether there is a gap in a jurisdiction’s exchange network. Several jurisdictions triggered this process. As a first step in the review process the Global Forum facilitates further bilateral engagement. As a result of this facilitation the bilateral engagement has intensified and the jurisdictions have decided not to move to the next step in the process, which is the full review process.

Criterion 3: Convention on Mutual Administrative Assistance in Tax Matters in force or having a sufficiently broad exchange network of bilateral agreements

Today 129 jurisdictions participate in the Convention on Mutual Administrative Assistance in Tax Matters (the Convention), resulting in over 6 000 exchange relationships. However, **one jurisdiction (Trinidad and Tobago) committed to AEOI still needs to ratify the Convention.**



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