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REPORT

on the Mini Symposium on International Tax Policy After Pillar One

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In the context of the academic ceremony in honor of the graduating Advanced LL.M. in International Tax Law class 2022/2023 which took place on 31 August 2023, the Amsterdam Centre for Tax Law of the University of Amsterdam hosted a Mini Symposium on International Tax Policy After Pillar One.

This report provides a summary of the discussions held by the panelists, followed by a few takes from the author.

Opening Remarks by Prof. Dr. Ir. Peter-Paul Verbeek (Rector Magnificus at the University of Amsterdam)

Verbeek began the session by focusing on the ethical challenges raised by the digitalization of the economy and the consequent need to review the international standards currently applied to allocate taxing rights between countries. He anticipated that the analysis developed in the context of this symposium deals with a responsible way to address disruptive societal changes like the digitalization of the economy, as part of the ongoing *scientification* of society and *societalization* of science. The increasing societal engagement of researchers and scholars requires responsibility and explicit ethical reflection.

Pillar One: Setting the Scene by Eric Robert (Senior Tax Advisor at the OECD)

As a basis for the discussions of the first panel, Eric Robert provided some introductory remarks on the status of the Pillar One initiative and its connections with the topic of digital service taxes (DSTs).

He reported that the OECD was very close to the finish line with the Multilateral Convention on Pillar One (MLC) and the signing ceremony was expected to take place by the end of this year.

According to Robert, the MLC is not to be intended as a simple mechanical income allocation device. The broader purpose of the MLC is indeed to restore stability in the international tax system by establishing a coordinated response to the current challenges raised by the digitalization of the economy.

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The MLC also addresses DSTs. The standstill and withdrawal commitment on DSTs is a fundamental piece of the overall project. Nevertheless, in the final version of the MLC there will not be significant changes on this aspect as compared to the Public Consultation Documentation released on 20 December 2022 by the OECD Secretariat. The standstill clause will be applicable on taxes characterized by the following design features:

(i) Market based taxes that seek to tax profits deriving from market factors;
(ii) Ring-fencing of the measure;
(iii) Not covered by double tax treaties.

The taxes excluded from the DST definition are consumption, transaction, and estate taxes. Also, specific anti-abuse measures cannot qualify as DSTs.

Guidance has been developed on the ring-fencing concept. The OECD has also developed a procedure to assess whether a measure can qualify as a DST under the MLC.

On 11 July 2023 many jurisdictions, including members of the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS), agreed to extend the DSTs moratorium to the earlier of 31 December 2024, or the entry into force of the MLC. This commitment is conditional upon signature of the MLC before the end of 2023 by at least 30 jurisdictions where at least 60% of the ultimate parent entities of the in-scope multinational enterprises (MNEs) are located. The Member States are also expected to commit to extend the standstill if the MLC does not enter into force by 2024. According to Robert, this is a good sign for the Pillar One project because it demonstrates that many States are committed to it.

Panel 1: Digital Services Taxes and How to Prevent Global Tax Chaos

Chair: Raffaele Russo (UvA/Chiomenti; former Head BEPS Project)

Pascal Saint-Amans (Université de Lausanne/Bruegel; former Director of the Centre for Tax Policy and Administration at the OECD)

Karine Halimi-Guez (Vice President-Head of Tax at Booking.com)

Eric Robert (Senior Tax Advisor at the OECD)

Rupal Maheshwari (Alumna Adv LLM Program/LBD)

Panel 1 focused on three main questions:

(i) Why do we have DSTs?
(ii) What are the main practical issues coming from DSTs?
(iii) What are the revenue implications of DSTs (also as compared to those potentially deriving from Pillar One)?

Saint-Amans started off by answering the first question. DSTs were introduced because of the frustration with the currently existing nexus and income allocation rules. Due to the digitalization, MNEs may have significant digital presence in the market jurisdictions without being liable to taxation therein due to lack of nexus. There may be material profits created from the generation of marketable data through the use of digital products and services. More in general, there may be *new* income categories deriving from *new* business models and those may not be captured by the existing sourcing rules. This phenomenon was also coupled with the concerns raised by aggressive tax planning because massive profits made out of specific territories were booked and taxed elsewhere.

A countermeasure might have been terminating tax treaties. But this would have had broader and probably unforeseeable consequences. Changing the rules would also have been a possible countermeasure but it would have required wide consensus, which is always difficult to obtain.

Therefore, according to Saint-Amans, the reason why we have DSTs now is ultimately to allocate more taxable revenues to market jurisdictions in order to solve the issue arising from the lack of consensus. Halimi-Guez argued that the frustration with existing treaties might have blurred the view and probably might have led to unintended consequences. Indeed, there are several theoretical and practical unsolved issues that make DSTs so undesirable in Halimi-Guez's view:

- *Definition*: the assessment of the three criteria mentioned by the "positive" definition in the MLC may lead to a tax that resembles very much a consumption/excise tax which however, based on the "negative" DST definition in the MLC, is not covered.
- *Scope*: DSTs are levied virtually on all types of intermediaries. However, the measure was initially supposed to target only those which derive profits from consumers data by trading (or otherwise using) them outside market jurisdictions.
- *Double or multiple taxation*: DSTs regulations often use terms like "clients" and "users" interchangeably. The reality is that, depending on the business model, these two can be very different from each other. For example, for digital travel platforms, "clients" are those with which the platform has an agreement (i.e., those providing accommodation services) whereas "users" are the travelers. However, the lack of distinction between the two by local DST legislations results in double taxation on the same economic transaction if the client and the user are in different jurisdictions.
- *Lack of safe harbors*: DSTs do not generally consider that MNEs might already have taxable profits allocated in the market jurisdictions.
- *Excessive taxation*: DSTs are taxes applied on gross revenues. It is not considered whether the company is profitable or not.

Halimi-Guez therefore concluded that DSTs are disproportionate measures. They may hardly contribute to the restoration of stability in the international tax system.

Nevertheless, countries may still be interested in keeping DTSs. This was very clearly highlighted by Maheshwari who focused on the revenue consequences of DSTs and concluded that jurisdictions can raise much more revenues through unilateral DSTs than with Pillar One. This was explained as follows:

- Differences in the delineation of the scope. Global annual revenue threshold of EUR 750 million generally provided for DSTs and EUR 20 billion threshold for Pillar One lead to differences in terms of States' revenues that can be derived from the two alternative measures;
- As per the latest OECD tax talks in July 2023, Pillar One will imply a reallocation of taxing rights from low-tax investment hub jurisdictions to high-tax market jurisdictions of USD 17-31 billion annually per year (based on 2021 data and expected to increase over time);
- These estimates can be compared to the actual/short forecast collection of DSTs by some states. U.K. estimates to raise up to GBP 3 billion by 2025. France has, over the period of four years, collected EUR 1.9 billion. Italy has, over the period of three years, collected EUR 9.28 million. India, over the period of six years, has already collected EUR 1.4 billion. Kenya has collected, over the period of four years, EUR 4.2 million. These five countries put together have collected/will collect closely EUR 7 billion. Many other countries, like Canada and New Zealand, started to introduce unilateral DSTs.

Yet, according to Maheshwari it is undesirable that countries implement unilateral DSTs because, due to the lack of a coordinated response, there would be multiple taxation, trade wars and ultimately tax chaos.

Moving towards the end of the panel discussion, Russo summarized the views expressed by the panelists and challenged them by showing an alternative way to look at DSTs as a *new* form of taxation which is completely unrelated to corporate profit taxation and is designed to provide taxing rights on any contribution to the value chain of MNEs coming from users, consumers or customers. The proxy of that value can be nothing but revenues, absent any other reliable type of indicator. This may overcome some of the arguments raised by the participants against the DSTs which may, therefore, be preferred to Pillar One in light of their ease of administration and revenue features. Also, the argument that DSTs are not desirable because they may be passed on to consumers should not be upheld. Indeed, all types of taxes paid by legal entities are ultimately passed on to the stakeholders (e.g., shareholders, employees, etc.).

By anticipating some of the discussions of the next panel, the participants finally expressed their view on potential alternatives to Pillar One, should the project not see the light of the day. The participants agreed that DSTs, as currently designed, cannot be considered as a viable solution to the international tax concerns. Therefore, participants did not generally see DSTs as the way forward. In any case, to become a real alternative to Pillar One, DSTs should be less disproportionate and more globally coordinated.

Panel 2: Other Solutions or Alternatives to Pillar 1

Chair: dr. Svitlana Buriak, (UvA/Loyens&Loeff)

Giammarco Cottani (Head of Tax, Agoda)

Daan Vreeman (Head of International Tax Affairs, Dutch ministry of Finance)

Anna Vvedenskaya (Alumna Adv LLM Program/UvA/EY)

Prof. Dr. John Vella (University of Oxford)

Panel 2 started from where we left off. Are there alternative solutions to Pillar One? Probably yes, but then how should these be designed?

Buriak asked whether ring fencing presents an issue, considering that the existing regulations might be suitable for conventional business models, whereas implementing new rules for these traditional business frameworks often lacks practicality. Since any new measure should focus on the digitalization of the businesses, we need to be able to delineate the concept of digitalization first. If we dig a little bit more in this, we however discover that digitalization may assume many different forms, such as: digitalization of the customer channel, digitalization of processes, use of customer data, digitalization of human resources involvement, and more. Therefore, the question is whether and how (if at all) is necessary to ring fence the digital economy from the rest of the economy for the purpose of designing a measure capable of addressing the tax challenges of the digitalization of the businesses.

In Cottani’s view the ring fencing is simply not feasible. This is because business models evolve constantly and increasingly faster. Also, a new measure with a narrower scope would probably not be perceived as “fair”, considering that the concerns revolving around the Pillar One project are not only related to certain types of digital business but also on the need for market jurisdictions to get access to at least some of the taxing rights on the table. This is demonstrated by the fact that many countries are already trying to establish market-based taxation on the basis of the currently existing nexus and transfer pricing rules.

According to Cottani, rather than trying to design a new and narrower scope, it is important to focus on the pros and cons of the Pillar One project. Broadly speaking:

(i) Amount A lacks ease of administration and requires changing domestic laws and international tax laws, and introducing the MLC;
(ii) Amount B seems key because it would fix some of the pressing issues of the current transfer pricing rules by determining how to remunerate marketing and distribution activities.

Any other solution, such as a standardized DSTs or a withholding tax for digital services, alternative to Pillar One, concluded Cottani, may be more effective than the current measures in avoiding double taxation. Tax treaty relief is, therefore, a key. Increasing VAT paid by MNEs in the market jurisdictions may be a solution but then the question arises as to whether that may be sufficient or not.

The panel further discussed whether there is the need to review the existing sourcing rules. According to Vella, we should reflect on the possibility to radically change the existing sourcing rules because the taxing rights are generally located where relatively mobile factors are located. The significant economic presence concept and formulary apportionment together with the profit allocation criteria were also discussed. Buriak and panelists addressed the potential introduction of the significant economic presence, that may prove exceptionally difficult because it would require a drastic change of the current architecture of international tax law and new nexus rules. Vreeman brought up formulary apportionment as one of the alternatives and asked to the panel whether turnover and employees are, in their view, good proxies to identify the value deriving from users. According to Vvedenskaya formulary apportionment is potentially a practical and simplified solution. However, it is hardly possible to find the perfect solution for a given very complex situation. The international tax community may in the end agree to a second or third best scenario.

Closing Remarks from Prof. Dr. John Vella

The mini symposium was concluded by three high-level observations from Vella:

(i) First, over the past ten years we have we have seen so many reforms. The introduction of CbCR, the substantive changes brought by the BEPS reforms, the rising of multilateralism and the creation of the Inclusive Framework, the developments in the exchange of information framework and the U.S. international tax reforms are only some examples. It is easy to forget how genuinely remarkable these reforms are and how they seemed almost impossible to achieve just a few years ago. We should not get so accustomed with such incredible reforms. This shows that ambitious international tax reforms are possible;
(ii) Second, considering the continuing pressure to reform the system, we might forget what the ultimate objective of the international tax system should be. The main objective should be to have a *good* tax system based on criteria like efficiency, fairness, robustness to abuse, and ease of administration. The objective of the proposed reforms should be to improve at least on some of these criteria. The suspect is that at least some of the proposed reforms may increase the complexity of the international tax system, that it is already very complex. This is because we continue to add layers up on layers on the existing rules. Complexity is a cost. And a genuine concern is that the complexity of the system is a source of instability;
(iii) Third and final point, the panel discussions have highlighted how political compromise is important to achieve successful tax reforms. However, one should not forget that the lack of clarity on principles underlying any of these reforms may lead to irrational changes which ultimately do not improve the international tax system.

Author's Take on Panels Discussion

The first panel discussion sounds like a huge call for multilateralism. Based on the various views, it can be argued that DSTs may not represent a viable solution if they are not conceived as global and coordinated actions. Cross-border problems may require cross-border solutions and individual measures only exacerbate the fragmentation of the legal framework causing inefficiencies, multiple and excessive taxation, complexity and, ultimately, chaos.

In addition, unilateral DSTs seem at odd with the recent evolution of the international tax policy:

(i) In September 2023, the OECD/G20 Inclusive Framework released the Multilateral Convention to Facilitate the Implementation of the Pillar Two Subject to Tax Rule (STTR MLI) to implement the Pillar Two Subject to Tax Rule in existing bilateral tax treaties without the need for bilateral negotiations;

(ii) In October 2023, the Inclusive Framework's Task Force on the Digital Economy approved the release of a text of the MLC, together with related materials (such as an explanatory statement). The text of the MLC, which is not yet open to signature, reflects the consensus achieved so far among members, with different views on a handful of specific items noted in footnotes by a small number of jurisdictions;

(iii) EU is further enhancing the multilateral dimension of its tax legislation. Indeed, the idea that a compensatory tax measure like Pillar Two may be imposed without violating EU freedoms seemed unconceivable years ago (see, e.g., *Eurowings*, Case C-294/97) and now we have a Directive that essentially establishes new taxing rights when other states do not make use of their taxing powers, irrespective of any consideration regarding territoriality (under a sort of "always somewhere" taxation principle often recalled during the LL.M. lectures last year). The recent initiatives put forward by the EU Commission and announced in the Communication on Business Taxation for the 21st century mostly follow the same trend. On 12 September 2023 the EU Commission adopted a key package of initiatives by delivering (i) a proposal for a Council Directive on Business in Europe: Framework for Income Taxation (BEFIT) (COM (2023) 532 final), to develop a common corporate tax framework, and (ii) a proposal for a Council Directive on Transfer Pricing (COM (2023) 529 final), to integrate the arm's length principle in EU law.

In light of the panel discussions, all these multilateral measures should be warmly welcomed, considering their objectives to level a playing field, enhance legal certainty, reduce complexities, and fight abuse. However, all these measures seem to share the same huge and perhaps currently unsolved issue: the absence of flexibility. Indeed, it may require constant changes to adapt to the evolution of the environment and to solve criticalities that may emerge from practice. At present there is no process in place to quickly gather consensus from states and to effectively amend rules. As some of the mentioned initiatives are currently designed, it may be argued that states can either accept OECD positions to remain compliant (see, e.g., recital 24 of the preamble to Pillar Two Directive on the relevance of the OECD Model Rules and related Commentary) or spend much effort on a permanent basis to continuously negotiate changes at the Inclusive Framework level. It remains to be seen how the debate will evolve on this which, in my view, may represent a crossroad between success and failure for multilateralism in the international tax policy.

The first panel noted how close DSTs are to consumption taxes. The second one mentioned them as potential alternatives to DSTs. During the first panel discussion, Russo described a very common pattern of modern online businesses: to access their services they give the choice to either providing customer data or paying a subscription fee. That involving customer data resembles very much a barter arrangement which already

represents a taxable transaction for VAT purposes under the existing legislation. There are indeed examples of tax audits in which the tax authorities are arguing that granting access to social networks in exchange of data from users is actually a VAT taxable transaction. Besides the several theoretical and practical reasons why this position may not be upheld, this naturally takes us back to the complex exercise of identifying a proxy for the value attributable to the input given by customers (or users). Accordingly, one may argue that the VAT solution is not as simple as it may look at first glance, although differently from new forms of taxation we can leverage on years of studies revolving around VAT.

Discussion on the value proxy issue and leveraging existing knowledge leads to a second reflection on a possible alternative to Pillar One: working on the arm's length principle (ALP) and expanding the existing notion of PE. Drafting additional TP guidelines for allocating income (also) to market jurisdictions and amending the existing BEPS Multilateral Instrument to introduce a concept of virtual PE seems not much more difficult to achieve than it is to introduce a brand-new multilateral convention (the MLC) which is effective alongside the existing ALP, after all. This solution would at least take away some of the concerns related to the need for coordination between the two systems such as the need to identify paying and relief entities and preventing 'double counting' in instances where a market jurisdiction can otherwise tax the excess profit by introducing safe harbors. However, the existing issues of the international tax framework would still remain unsolved. For example, it would be necessary to get further clarification on the meaning of the notion of "value creation" and on how such notion should be used for the operation of the ALP. Also, much more work for refining transactional net profit split methods would be necessary, considering that this would be widely used due to the highly integrated and global nature of digital value chains.

To sum up, the discussion highlights that there is plenty of alternative solutions that may be implemented to change the current shape of the international tax system. Some are just ideas and others are the object of reforms that are progressing quite fast. However, as also mentioned by Vella, what is probably more important at this stage is to try to get clarity on the exact purpose of any of the step taken to reform the international tax system. Otherwise, we would continue adding layers to existing systems, which ultimately lead to complexity and chaos.