“BUILD YOUR HOUSE ON YOUR OWN PILLARS”

Key Issues for Developing Countries at the OECD Inclusive Framework Negotiations

Profitability and allocation of taxing rights to market jurisdictions

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Profitability and allocation of taxing rights to market jurisdictions

Based on current standards on international taxation, jurisdictions are allocated to taxing rights on business profits attributable to permanent establishments located therein in accordance to the arm’s length principle.

Consequently, in the absence of a permanent establishment, jurisdictions are not allowed to tax business profits generated therein.

Pillar One of the IF Global Solution to address the tax challenges of the digitalized economy seeks to allocate taxing rights to jurisdictions where profits are generated in the absence of physical presence.
Profitability and allocation of taxing rights to market jurisdictions

The new Amount A is being designed in a way that in-scope MNEs would be subject to taxation in market jurisdictions on a portion of their global non-routine profits.

Non routine profits are considered to be those in excess of routine profits, meaning the profits that, according to the arm’s length principle, remunerate functions performed, assets involved and risks assumed in the business activities.

By virtue of simplification, routine profits would be deemed to be a specific portion of the total profits. Such portion has not been decided yet, but it is expected to be around a profitability margin of 10% or 15% on gross revenues.
Profitability and allocation of taxing rights to market jurisdictions

A portion of the non-routine profits (the **reallocation percentage**) would be subject to tax in market jurisdictions.

Such reallocation percentage has not been decided yet but it is expected to be around 15% or 30% of the non-routine profits.

Any single jurisdiction that meets the nexus requirement would be allowed to tax the portion of the non-routine profits that are allocated to market jurisdictions, in proportion of the gross revenues derived by the MNE Group from such jurisdiction.
Profitability and allocation of taxing rights to market jurisdictions

- Routine profitability
- Non-routine profitability

Profitability margin of 10% or 15% on gross revenues

Re-allocable portion of the non-routine profits that would be subject to tax in market jurisdictions following a formulary apportionment
Profitability and allocation of taxing rights to market jurisdictions

According to the current structure of Amount A, in order to increase the tax base and provide an equitable tax treatment, developing countries favor:

- a **low threshold of global revenue** to determine MNEs subject to Amount A;
- a **low profitability ratio** to determine routine-profits;
- a **high reallocation percentage** of the non-routine profits;
- a **low threshold of gross revenues** from a market jurisdiction to trigger the nexus.

However, following the views of some developing countries, the re-allocable percentage should apply on the global profits and not just on the non-routine ones. This the criteria followed under Article 12B of the UN Model Tax convention.
THANK YOU

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