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South Centre Comments on the 'Amount A Draft Multilateral Convention Provisions on Digital Services Taxes and other Relevant Similar Measures'

I. Background

The South Centre is the intergovernmental organization of developing countries that helps developing countries to combine their efforts and expertise to promote their common interests in the international arena. The South Centre has 55 Member States coming from the three developing country regions of Africa, Asia, and Latin America and the Caribbean. It was established by an Intergovernmental Agreement which came into force on 31 July 1995. Its headquarters are in Geneva, Switzerland.

The South Centre in 2016 launched the South Centre Tax Initiative (SCTI). This is the organization's flagship program for promoting South-South cooperation among developing countries in international tax matters.

The South Centre submits the following comments and recommendations to the OECD Inclusive Framework's Task Force on Digital Economy (TFDE) on the Draft Multilateral Convention Provisions on Digital Services Taxes and other Relevant Similar Measures.

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II. Comments and recommendations

i. Article 37: Removal of Existing Measures

a. Blanket ban on Existing Measures

Article 37 (1) states that the measures listed in Annex A (List of Existing Measures Subject to Removal) cannot be applied to any company at all, not just those in-scope of Amount A. This blanket ban is one of the most egregious and unfair aspects of the Amount A rules.

Recommendation: The ban should apply only to companies in-scope of Amount A.

b. Unilateral Measures on Companies Headquartered in Developed Countries

Footnote 2 discusses the question of whether unilateral measures can continue to be applied on Multinational Enterprises (MNEs) with Ultimate Parent Entities (UPEs) in jurisdictions that do not implement Amount A. This is a welcome proposal as unless these countries join the Amount A MLC, there will be no taxes to be redistributed. Thus, their participation is essential for the Amount A mechanism to work, or it would mean only that developing countries would give up their taxing rights and get nothing in return. The proposal will therefore incentivize countries where the tech giants and other major in-scope companies are headquartered to join the Amount A MLC.

Recommendation: Unilateral measures must be allowed for MNEs with UPEs in jurisdictions that do not implement Amount A.

ii. Article 38: Provision Eliminating Amount A Allocations for Parties Imposing DSTs and Relevant Similar Measures

a. Measures by subnational governments

Footnote 3 discusses the question of whether and how Digital Service Taxes (DSTs) and other relevant similar measures imposed by subnational jurisdictions should be addressed. Digital Service Taxes are at present imposed by subnational governments, including those of the developed countries. For example, the USA, which has threatened unlawful unilateral coercive measures such as the 301 trade sanctions on countries for exercising legitimate tax policy and implementing DSTs, itself imposes DSTs at the subnational level, such as in the state of Maryland. These are now treated

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as Covered Taxes in some bilateral tax treaties and are creditable[1], with the net result that sometimes developing countries have to give foreign tax credits to the MNEs of developed countries. Whether the tax is implemented at the federal or state level does not seem to make a major difference for the purposes of avoiding international double taxation.

Recommendation: For these same reasons, DSTs and other similar measures by subnational governments should be included in the prohibited measures. It would also avoid the negative scenario where developed countries reject their own prohibition and implement DSTs at the state level citing federalism and constitutional limits.

b. Denial of Amount A allocation

Footnote 4 for Article 38(1)(a) discusses "whether full denial is appropriate in all circumstances, or whether denial should be in some respect proportional to the scale of the offending measures".

It is unfair to apply full denial. For instance, there may be a scenario where a Party is entitled to an Amount A allocation of USD 10 million, but adopts a measure that has a tax impact of only USD 1 million. This rule would mean its Amount A allocation will become zero.

Applying the proportional approach on the other hand would mean the Amount A allocation will only be reduced by USD 1 million. This is more sensible and in line with the objective of avoiding double taxation.

Recommendation: Denial should be proportional to the scale of the offending measures.

c. Definition of Measures: Market-based criteria

Article 38 defines DSTs and relevant similar measures, which must meet all **three** criteria. 38(2)(a) states, "the application of such tax, or the amount of tax imposed, is determined primarily by reference to the location of customers or users, or **other similar market-based criteria.**"

[1] https://facelesscompliance.com/12132/assessee-entitled-to-tax-credit-of-usa-federal-as-well-as-state-taxes-u-s-91-itat

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The phrase "similar market-based criteria" is vague and can open the floor for disputes over what measures are covered.
Recommendation: Phrase "similar market-based criteria" in 38(2)(a) should be deleted, or criteria specified in the Article itself.

d. Definition of Measures: Non-residents

Whatever the theoretical objection to non-discrimination may be, the reality is that for several developing countries they have no real domestic alternative to companies such as Google, Facebook, Twitter, etc. These sectors of their economies are dominated by the tech giants. Attempts to tax them are bound to target non-residents.

Recommendation: The technical definitions of non-residents and foreign owned businesses must keep in mind this reality of developing countries.

e. Definition of Measures: Tax Treaties

Footnote 10 to Article 38(2)(c) discusses "whether and under what circumstances the definition of digital services taxes or other relevant similar measures should **cover certain measures even if they are within the scope of existing tax treaties**."

This is an illogical, unjustified and dangerous proposal that ostensibly seeks to prevent countries from pursuing legitimate alternative policy solutions, especially by the United Nations, to taxation of the digitalized economy. In practical terms, it may be used against Article 12B of the UN Model Tax Convention (Income from Automated Digital Services). Thus, even if two countries include Article 12B in their bilateral treaty, it would be treated as prohibited if it meets the other two criteria.

There is no reason why taxes covered under existing bilateral tax treaties should be included in the scope of prohibited measures. It goes against the fundamental sovereign right of countries to decide their tax policy for themselves.

Recommendation: Proposal to cover measures even within scope of existing tax treaties should be strongly and completely rejected.

f. Determination if measures still in effect

Article 38(4)(b) states "a Party shall be considered to have a digital services tax or relevant similar measure in force and in effect if… the Conference of the Parties has

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not determined that the Party has withdrawn that measure or otherwise terminated its application with respect to all companies."

The wording of this implies that the Conference of Parties may have to determine in each instance whether a measure has been lifted. This is a cumbersome and dispute prone process.

Recommendation: Notification of termination by the Party can be considered sufficient, unless objected to by another Party(ies) to the MLC.

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