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Pillar One – Amount A : Draft Model Rules for Nexus and Revenue Sourcing

The participant[1] thanks the OECD for the opportunity to provide comment on part of the process of updating international tax rules to a digitalized economy. The draft seems to include most digital business models that cause tax issues by facilitating base erosion and profit shifting. This by allocation of the collection of revenue outside the market jurisdiction and/or locate part of the digitally organised economic activity outside that jurisdiction.

1.

The <u>first topic</u> for input considers that the rules of allocation of revenue will be used as criteria to shift reported profits among jurisdictions. The choice for the criterion of allocating revenue is welcomed by the participant.

Especially the allocation factor 6.B for revenue retrieved from user data to that users' jurisdiction tackles effectively one of the major concerns digital business models pose by absence of need of physical presence for their economic activity in a jurisdiction. The participant strongly hopes that this rule will still be included in the final recommendations the OECD will issue on Pillar I.

Revenues retrieved from user data express that wealth is created by harvesting these data. Be it as a primary objective in a business model that offers free services to users or as a secondary objective when users of that jurisdiction make choices on the group's websites. A same group may venture in multiple digital business models, but for effectiveness purposes the revenue retrieved from selling user's data should be singled out and not follow the rules of allocation of revenue from the underlying economic activity. The draft enters in that logic by proposing that revenue is to be designed to an activity in scope before applying the rules of allocation for revenue per type of activity.

Some may plead against factor 6.B by saying that there is no need for any form of physical activity in the market jurisdiction for harvesting user data and this factor must not be split from the type of economic activity the user is engaged in. Others may object that this rule of allocation is in violation of tax treaties for as long as both jurisdictions have not joined in and adopted in national law the multilateral instrument the OECD is yet to draft.

The participant responds that harvesting user data forms a separate economic activity since it relates to other buyers then those engaged in the underlying economic activity. As an economic activity that occurs constantly in the user's jurisdiction through active cookies on the tools of connection of the user, this activity gives cause to a fixed establishment under the existing tax treaties. The Resolutions of 20 December 2018 of the General Assembly of the United Nations # 73/203 on *Identification of customary international law* and # 73/202 on *Subsequent agreements and subsequent practice in relation to the interpretation of treaties*, to be read for full understanding of its meaning with the Report of the INTERNATIONAL LAW COMMISSION, Chapter IV Yearbook 2018, demand a combined interpretation of criterions (textual, historical, teleological, clearly absurd or inequitable result) in good faith of tax treaties.

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[1] The participant **:** Paul Verhaeghe is a Belgian tax lawyer who has practiced tax law since 1998 with the Dutch speaking Brussels Bar Association. Since 2018 he is a member of the board of directors of the Belgian Association of Tax Lawyers that represents around 150 members. He provided input (88 p.) on the Secretariat Proposal for a "Unified Approach" under Pillar One. Public consultation document 9 October 2019 – 12 November 2019, the USTR requests for public input on the Initiation of a Section 301 Investigation of France's Digital Services Tax – Written Submission - [Docket No. USTR–2019–0009] – August 19th 2019 (28 p.), the Initiation of a Section 301 Investigations of Digital Services Taxes in Austria, Brazil, the Czech Republic, the European Union, India, Indonesia, Italy, Spain, Turkey, and the United Kingdom. Written Submission - [Docket No. USTR–2020–0022] (28 p.) and the U.N. Committee of Experts on International Cooperation in Tax Matters request for public input - Doc E/C.18/2020/CRP/10 - Update of the UN Model Double Taxation Convention between Developed and Developing Countries – Proposed changes to the Commentary on Article 5 (Permanent Establishment) – August 9th 2020 (30 p.).

Under these rules of interpretation, a fixed establishment for a company is present in a jurisdiction when a constant form of economic activity by that company occurs and this activity creates wealth for that company. The form that such economic activity takes to create wealth is irrelevant under these rules of interpretation when applying in good faith the combined criterions of interpretation.

The benefit and the ability to pay principles are commonly considered as objective criterions for equitable taxation in an international setting. Even a purely digital activity such as mining user data occurring in a jurisdiction has need of publicly organised services that relate to organising telecommunication and providing electricity to feed both the telecommunication network and the user's tool of connection. Under the benefit principle this need provides a rationale for allocating part of the revenue retrieved from user data in the user's jurisdiction. Under the ability-to-pay principle, the draft sets a sufficiently high nexus for revenues to justify taxation under that principle.

On the level of States, when the recommendations or the multilateral instrument of the OECD are not transposed by some jurisdictions or not in a timely or otherwise effective manner, the issue remains on how the market jurisdiction may respond to this under the existing framework of tax treaties. The said rules of interpretation allow a remedy in accordance with the rule of law for the market jurisdiction to tax the economic activity of harvesting user data in its territory. Provided it considers a similar nexus for revenue from that economic activity as in the draft.

On the level of companies, the regional and global keys that are yet to be determined by the OECD will be in the participant's view proof crucial for effective taxation when companies do not provide data on user activity or no reliable / verifiable data for categorizing revenue to one activity in scope and particularly that activity. These regional and global keys are best determined by criterions that measure the size of the digital activity through the number of identified users (subscribers or simply registered users) and connections to the group's websites (cookies etc..) occurring in a jurisdiction. They form pertinent criterions under the benefit principle to determine a constant form of economic activity when set proportionate to that jurisdiction importance in population and GDP. With the nexus such criterions are in the participant's view compliant with the existing network of tax treaties under the customary international law on the interpretation of treaties.

2.
The <u>second topic</u> of input relates to factor 5.D.5, the passenger non-air transport services. The proposed factor places some of the revenue in the jurisdiction of the place of destination. The participant understands that this factor will only apply when the revenue nexus of that jurisdiction is reached. There is rationale for that since reaching that revenue nexus requires a constant form of activity by organizing frequently repeated travels to that jurisdiction. It implies making frequent use of the roads or railways and other publicly provided services that justify that some of those public costs are supported by all those using them.

It is however unclear for the participant how part of the revenue will be allocated to that destination jurisdiction under factor 5.D.6, since the payment will typically occur in the jurisdiction where the transportation is booked. Does the wording of this factor imply that all revenue collected in the jurisdiction of the place of origin must then be disregarded? That seems not propionate under the benefit principle unless only a portion of the profit reported in the jurisdiction of origin is to be split. The factor under 5.D.7 for Cargo non-air transport services seems how evermore equitable for the participant by splitting the revenue between both jurisdictions. The Commentary should best provide rationale why both similar types of services are so different that they must be treated differently.

3.
The <u>third and last topic</u> relates to a branch of the digitalized economy that is particularly revolutionizing and intriguing. Tokens are increasingly interfering in economic activities, but the draft of rules seem not to give specific considerations on that type of economic activity. This seems logical since the companies in scope would not present their group's profit in tokens and the proposal is about shifting reported profits among jurisdictions. But when in the process of updating rules of international taxation, some thoughts

should be given to them since it is still unclear how fast their impact may grow on economic activity in general. This especially when an economic activity through tokens exceeds the nexus of revenue in a jurisdiction.

Tokens pose questions for measuring revenue. Issuers of tokens are basically bartering them against legal currencies, cryptocurrencies, or other tokens. In turn they offer some form of return to the person that gives that token in payment to them or a third party. You can quantify them by terms of revenue by evaluating the counterpart they are bartered for or when they take the form of cryptocurrencies with worldwide ratings in legal currencies.

There are for instance platforms that monetize commercial debts. They organize a market open for interested parties to bid with the issued tokens of that platform on the future income of the commercial debt. These tokens are issued against legal currencies or cryptocurrencies. The company owning the commercial debt receives the tokens it can barter with the platform for legal currencies. When the commercial debt is later collected, that company must buy issued tokens to render the bidders in tokens the full worth of the collected debt. That whole economic activity strikes the participant as an alternative form of factoring that may fall under the factor 5.F, that of non-regulated financial services. But which rules of allocation should be referred to under that factor for that type of activity? The draft specifies that the wordings of that factor may still change after the carve out for regulated financial services is specified.

Basically, tokens require wallets for bartering or changing hands. The companies that offer these wallets or keep records on them on their own platform can be established in another jurisdiction then the holder and the person willing to monetize the commercial debt through the highest bid on that flatform. Should that platform be on principle captured under the existing factor 5.C, revenues from online intermediation services? And how to capture the revenue that forms the capital gain for the highest bid that receives as counterpart the full commercial debt when collected?

The participant recommends that in further works some consideration is given to complex quadrilateral (wallet, issuer, holder, taker) digital business model, by allocating part of the revenue to the jurisdiction where the company is established that holds the wallet, the jurisdictions that holds the issuer of the token, its holder and the taker that is interested to acquire the token by offering a counterpart.

The participants whishes the OECD swift progress in its undertakings regarding Pillar I.

Sincerely, February 16th, 2022.

P. Verhaeghe