



Trade Union
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OECD Public Consultation on the tax challenges of the digitalisation of the economy (proposal for a “unified approach”) - Comments by the TUAC

Paris, 12 November 2019

The TUAC welcomes the opportunity to contribute to the OECD [public consultation](#) on the Secretariat Proposal for a "Unified Approach" under Pillar One and as discussed by the Task Force on the Digital Economy (TFDE) of OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting. This consultation follows the publication in February 2019 of four proposals to address the tax challenges of the digitalisation of the economy.

In its [response to the February consultation](#), TUAC supported the OECD efforts to address the tax challenges of the digital economy. TUAC recommended that governments reach a consensus based on long-term principles for fair taxation, as opposed to short-term trade-related considerations. TUAC recalled its support for unitary taxation, according to which groups of companies are treated for what they are: unitary world-wide entities, as opposed to an aggregation of distinct and autonomous entities.

The following includes TUAC reactions to the proposed “unified approach”, following an internal consultation of its members. TUAC agrees to the publication of this response.

General comments

Tackling tax avoidance is of high relevance to workers. In a context of austerity and budgetary constraints, the under-taxation of multinationals has an adverse impact on the sustainability of social protection regimes and may lead to regressive taxation as the tax burden is being shifted to consumers and workers.

Aggressive tax planning also entails aggressive social planning. Artificial constructions, such as shell companies and other letterbox-type practices, obscure employment relationships. Employers' liability becomes difficult to enforce. Profit shifting also negatively affects profit levels of otherwise profitable companies, thereby hampering investment in productive capacities and wages.

In its [2016 assessment of the BEPS package](#), TUAC has been highlighting a number of shortcomings of the current BEPS rules, including the prevalence of transfer pricing rules and the failure to account for the unitary dimension of multinational enterprises. The

transfer pricing guidelines are complex and difficult to implement in an effective manner. Above all, by treating subsidiaries and establishments as if they were autonomous entities, the current transfer pricing rules constitute an incentive for multinational enterprises ('MNEs') to fragment their group structures in order to shift profits from high tax jurisdictions to relatively lower tax jurisdictions. These inherent weaknesses are further exacerbated in the context of the digitalisation of the economy, as usefully described by the OECD in its 2018 interim report.

There is a need to revisit the current architecture in order to leave more space for unitary taxation. Profits should be determined at global level and allocated between countries according to a repartition key, reflecting all the factors of production of the MNE.

Revised allocation rules must go hand in hand with global efforts to stop the tax rates competition. The GLoBE proposal of pillar 2 could serve as a floor against tax competition, and has to be considered as an indispensable complement to pillar 1. The design and impact assessments of the two pillars must not be considered in isolation.

Finally, TUAC has expressed concerns about the lack of transparency on businesses' tax practices. Workers' representatives need to have access to information on the financial and economic situation of their company. Data on country-by-country reporting should be made publicly available.

General comments to the proposed unified approach

The proposed "unified approach" heads in the right direction because it recognises that introducing unitary taxation is unavoidable in an increasingly digitalised economy. However, the foreseen changes are too timid and, in practice, fall short of what is required to achieve fair and sustainable taxation.

The proposed "unified approach" would require companies to make greater use of unitary taxation, but this would apply to a small and in fact unclear part of profits and would rest upon undefined or un-tested concepts - "routine" and "non-routine" profits, "consumer facing businesses", etc. The instability created by these new and unstable concepts could encourage further accounting manipulations. In practice, this means that, far from addressing the problem of corporate fragmentation and its adverse impact on workers' rights, the proposed reform could actually worsen it.

Furthermore, the unified approach puts much emphasis on sales for the triggering of taxing rights. Sales are only one factor of production. A "sales-only" criteria tends to favour importing countries with large consumer markets to the detriment of developing economies as well as exporting models. All factors of production should be given appropriate consideration, including in particular employment, tangible assets, and sustained interactions with customers.

Overall, TUAC recommends that the Inclusive Framework reach a consensus on the basis of long-term principles. Governments might be tempted to refer to their current trade balances in order to assess the immediate impact of the proposed reform on the allocation of taxing rights. Short-term "winners/losers" considerations should be put in a

broader perspective. The dynamic effects of the reform in the longer run should as much as possible be anticipated. The introduction of new concepts lacking legal and economic foundations could indeed increase legal uncertainty and open the door to further accounting manipulations and arbitrary tax decisions. Concerning possible losses of tax revenues, it is important to try to also quantify the amounts which are today lost due to profit shifting and tax competition between countries.

Next steps

In order to reflect on long-term perspectives and alternative scenarios, TUAC recommends that the Inclusive Framework undertake the following next steps.

- Ascertain whether each concept under discussion (such as “non-routine” profits and “consumer facing businesses”) is founded on well-established legal principles and/ or on sound economic rationale.
- Step up impact assessment so as to include different scenarios for reform. The impact assessment should not be limited to the proposed unified approach but also assess greater switch to unitary taxation, as well as allocation keys reflecting all production factors.
- Attempts should be made at quantifying profit shifting after 2015.

Overall, making data on country-by-country reporting publicly available would ensure that all governments, OECD and developing countries, and all stakeholders can access the same level of information and make an informed assessment of the different proposals for reform. More transparency on tax practices is the best way to ensure trust and evidence-based decisions.

Comments on the specific issues

Scope

The unified approach would introduce the new concept of “consumer facing businesses”. This new concept would have a wider scope than the well-known “business to consumer operations”. The objective is to encompass not only business to consumers operations, but also business models using digital technology to develop a consumer base, as well as online platforms, which interact with users who are not always individual consumers.

TUAC is concerned about the introduction of important yet unclear and untested concepts. These could bring about unintended effects and will be the source of disputes.

Furthermore, it is not clear what justifies creating parallel tax regimes. As a response to the proposed “user participation proposal”, TUAC had already cautioned against the ring fencing of the digital economy. A limited application of the new rules to digitalised businesses would only amount to a partial solution to the need of a fundamental rethinking of the international tax rules.

Concerning the size limitation, a EUR 750 million revenue threshold is being suggested. Whilst the introduction of scope limitations may be understood for reasons of administrability, and would be consistent with the 2015 BEPS Action n°13 on country by country reporting, the current economic reality must also justify these thresholds. Such high threshold would exclude the majority of MNEs and would lead to indirect discrimination, as mostly non-European MNEs would be covered¹. The European Trade Union Confederation has taken position in favour of a EUR 40 million threshold for the application of unitary taxation. This threshold corresponds to the scope of the EU annual accounts Directives².

Finally, carve outs should be strictly limited. Exemptions should only be considered to the extent that they are justified by clearly defined social objectives, such as responding to the needs of developing economies.

Both size limitations and carve outs should be periodically reviewed.

Nexus

TUAC welcomes the proposal to adapt the nexus rules to the digitalisation of the economy. TUAC recommends that nexus is based on a flexible range of criteria reflecting the full economic activity of the MNE. For instance, according to the “significant economic presence proposal” a range of factors, including user base and local activities such as billing and support services, would be considered as relevant for constituting purposeful and sustained interaction with a jurisdiction. Sales are an important indicator, but on its own (as suggested by the unified approach) it tends to favour importing countries with large consumer markets to the detriment of other jurisdictions.

Calculation of group profits

Consolidated financial statements are likely to be the only available reference to determine group profits. For the sake of consistency, Action 13 should be adjusted to these new considerations. It will then be even more important to make country-by-country reporting public, so as to ensure transparency and public oversight.

TUAC has some concerns about calculating profits on the basis of segments based on business lines. Parent companies are already presenting segmented accounts as annexes to the consolidated accounts. These segments are being determined at the sole discretion of the company. A particular choice of segmentation is often made in order to present results in a favourable light.

If segmentation can have an influence on the overall level of taxation, businesses will manipulate even more their choice of segmentation for tax planning purposes. The risk of manipulation would be particularly pronounced if regional profitability is allowed, thereby defeating the primary purpose of trying to determine profit at group level.

¹ R. Mason, L. Parada, “digital battlefield in the tax wars”, November 2018, [Virginia Law and Economics Research Paper No. 2018-16](#)

² [ETUC position on the CCCTB](#), October 2016

Amounts A and B

The proposed unified approach would introduce a new distinction between the moving concepts of “routine” and “residual” profits. Again, TUAC warns against introducing untested and hard to stabilise concepts into the international tax architecture. Far from addressing the problem of accounting manipulation and corporate fragmentation, and its adverse impact on workers’ rights, the unified approach could actually worsen it.

The unified approach proposes to get around the problem of unclear definition by fixing a proxy for the determination of residual profit. Another percentage would then be fixed to determine the amount actually subject to the new profit allocation rules.

The unified approach may in the short-term increase for some jurisdictions the effective tax rate of highly digitalised businesses. This policy choice, however, comes at the cost of extreme complexity, arbitrary rules and legal uncertainty.

Amount B seeks to a certain extent to respond to national concerns about the weaknesses of the current transfer pricing rules by assigning a minimum amount of returns to marketing jurisdictions. Rather than addressing the weaknesses of the current international tax architecture, amount B adds another layer of complexity to the current rules and constitutes a potential source of arbitrary decisions and disputes.

Amounts A and B should be replaced by a unitary taxation system, whereby the profits of a group of company would be determined globally and allocated in accordance to standards allocation keys. Such reform would be simpler to implement and reflect more accurately the economic reality of multinationals.

Amount C

Stepping up dispute resolutions is a natural response to the introduction of moving concepts and arbitrary proxies. A simpler unitary taxation system would reduce the need for Amount C.

As a general rule, sufficient attention should be paid to the excessive reliance on secrecy in dispute resolutions. The choice of arbitrators and other procedural safeguards that are often lacking in private justice should also be a source of concern.