PWYP NORWAY
Making Transparency Possible

To:	Task Force in the Digital Economy (TFDE)
From:	Publish What You Pay Norway (PWYP Norway)
Date:	5th March 2019

Re: Input from Publish What You Pay Norway on the possible solutions to the tax challenges of digitalization

1. Disadvantages national companies have in comparison with multinational companies

We refer to the invitation for comments to the Public Consultation Document "Addressing the Tax Challenges of the Digitalisation of the Economy" as part of the Base Erosion and Profit Shifting Project. The consultation period ends March 6, 2019 and our comments have been sent to tfde@oecd.org before this date.

Publish What You Pay Norway (PWYP Norway) is an organization that has as its specialty to provide solutions in the areas of transparency and taxation. PWYP Norway has 20 member organizations and is part of the wider Publish What You Pay organization with more than 700 member organizations from more than 50 countries.

PWYP Norway has since 2011 done extensive research into the mechanisms that can be used in the tax area to secure fair and equitable taxation without any country trespassing on the tax base of other countries.

PWYP Norway and other organizations in Norway has made input to the Norwegian Bank Investment Management (NBIM) expectation document on Tax and Transparency[1] which state "Appropriate, prudent and transparent tax behaviour is a key component of corporate responsibility" and the expectation is that "taxes should be paid where economic value is generated".

Economic value is generated in three places:

- In countries where non-renewable or renewable resources are produced,
- In countries where products are manufactured or services are created,
- In countries where products and services are sold.

[1] Tax and Transparency Expectations Toward Companies, NBIM 2018, https://www.nbim.no/contentassets/29f69f7ae81449f9adc88a32aa3de8c8/expectations-document---tax-and-transparency---norges-bank-investment-management.pdf

Any other countries that are introduced in the value chain between resources and end-customers are intrusive elements encouraged only through market failure, including harmful tax competition between countries. These intrusive elements introduce inefficiencies in the use and reuse of global resources, demonstrated amongst other through that the audit trail of invoices are different from the optimal logistical route of the resources and the resulting products. If the use of the world's resources is going to be sustainable, the taxation of multinational companies needs to be organized such that multinational companies does not have a competitive edge over national companies due to the tax arbitrage possible using intrusive elements in the value chain.

National companies have the following disadvantages compared to multinational companies, disadvantages that has to be overcome if national and multinational companies are to compete equitably with each other:

- **Information disadvantage:** national companies provide key numbers on their activities through their financial statements. However, when multinational companies provide their financial statements, these financial statements are aggregated to such an extent that country-information cannot be deduced from these statements. This information disadvantage can only be overcome by having all multinational companies report extended country-by-country information in order for key information in their financial statements being available on a country by country basis. PWYP Norway is not in favour of having OECD BEPS country-by-country reporting to tax administrations made public. The CBC reporting of taxes and other information to tax administrations has to develop over time catering to the needs of tax administrations, while an extended country-by-country reporting to the public needs to cater to information that is important to investors, statistics, politicians, media and the broader society. An extended country-by-country reporting should thus include such measures as (minimum) number of employees (of FTE's), production by type (if producing non-renewable or renewable resources), investments, revenues, costs and taxes paid (consisting of tax liability 1.1. and 31.12 and taxes payable from current year P&L).
- **Tax disadvantage:** national companies are at a competitive disadvantage compared to multinational companies due to the latter's introduction of intrusive elements (companies in low- or no-tax jurisdictions that are not part of the logistical operation) into the value chain which results in a significant tax leakage from countries with legitimate tax claims (resources, production or sales) to countries without any legitimate tax claims other than the continuation of harmful tax practices built up over the last 100 years. The distinction between illegal tax evasion and legal tax avoidance is in this setting outdated and irrelevant for equal competition purposes. The remainder of our comments thus addresses the tax disadvantage itself, not the causes of the tax disadvantage, and that the end result desirable is to end the unequal competition that we currently experience between national and multinational companies due to the tax arbitrage multinational companies enjoy.
- **Accounting disadvantage:** Some companies can under existing rules adjust balance sheet items using fair value adjustments while other companies have few such adjustments they can make. This results in that some industries and some companies seem relatively more attractive than other industries and companies, just because they are able to include unrealized values in their equity and are able to dividend funds to a higher degree than these other industries and companies. However, fair value

adjustments have only an information value for investors desiring to put their money into companies. Besides this aspect, any fair value adjustments by some industries and companies compared to other industries and companies only introduces distortions in the competition for funding of different industries and companies. In order to secure the information value of fair value adjustments to investors while at the same time secure that fair value adjustments do not introduce distortions in the competition, any fair value adjustments done should (1) not affect the profit & loss statement (but be a balance sheet adjustment only) and (2) be captured in a separate part of the equity that cannot be used as dividends or otherwise be viewed together with other parts of the equity which is based on realized earnings.

2. How to solve the tax disadvantage national companies have

If we then focus on the tax disadvantage that national companies have compared to multinational companies, **it is easy to demonstrate that the competitive disadvantage national companies have is connected to the ability multinational companies have to relocate their tax base to low- or no-tax jurisdictions using internal cross-border transactions. If the problem is internal, cross-border transactions, then the solution must be how to tax these internal, cross-border transactions.**

Many people, even tax professionals, only uses one typology, transfer pricing, for the valuation of these transactions, but this effectively disguises the very varied nature of these internal, cross-border transactions and the type of abuses going on. PWYP Norway has through its research expanded the typology to the below categories, and once broken down it is possible to correctly identify the possible solutions how to secure that nationals and multinationals can compete on an equal footing without any tax arbitrage distorting the competition.

The transactions whose valuation method is usually termed as transfer pricing can be broken down into the following types with their corresponding undesired effects and the identified counter-mechanisms to these undesired effects:

Transactions	Undesired effects	Counter-mechanisms
Derivatives	Derivative abuse	Derivatives in a separate tax base
Capital gains	Capital gains abuse	Derivatives in a separate tax base
Mark-to-market	Mark-to-market abuse	Reverse tax credit
Non-transactional cash flows	Valuation abuse	Reverse tax credit
Tax regulation transactions	Valutation or pricing abuse	Reverse tax credit
Internal transactions	Pricing abuse/mispricing	Reverse tax credit
Re-directed income	Countering tax systems	VAT and withholding tax
Cross-border B2C sales	Countering tax systems	VAT and withholding tax

Once broken down this way, it effectively shows that three counter-mechanisms can be introduced covering the relevant sub-types of transactions in order to secure that one can avoid undesirable effects and hence secure equal competition between national and multinational companies – unaffected by any tax arbitrage secured by the multinational company in their use of low- or no-tax jurisdictions in their value chain.

Derivatives

Derivatives have their own decision processes, their own contracts, their own accounting rules and they should also have their own taxation rules. Derivatives can be used for hedging or for speculation. The medium to long-term expectation for use of derivatives for hedging purposes is zero or slightly positive economic outcome (or else it would not make sense to use hedging). Moving derivatives into a separate tax base, separate from the company's general tax base, will result in that companies can continue to use derivatives for hedging, but it becomes uneconomical to use derivatives for speculation unless the speculation goes on in the same country so that there is a balanced loss and profit expectation for the speculative use of derivatives. Having derivatives in a separate tax base makes it impossible to plan for having derivative losses in high tax countries and the opposite revenues in a low- or no-tax jurisdiction.[2]

Capital Gains

Capital gains is one of the areas where companies may try to secure that the capital gains are converted into something else in order to secure that the taxation of the capital gain is going away partly or completely. One of the ways capital gains can avoid taxation is to combine capital gains with derivatives. Hence, moving derivatives into a separate tax base, so that the tax effects of derivatives cannot be combined with the tax effects of any capital gains, is one of the easiest ways to secure a better and more balanced taxation of capital gains. The same considerations as for derivatives are applicable here, but the consequences of combining capital gains and derivatives to create lower taxation of capital gains can have incredibly large consequences as capital gains tends to be very high relative to regular business-as-usual revenues.

Mark-to-market

Mark-to-market is a concept whereby transactions are valued against fluctuating market rates or assets are adjusting against fluctuating market rates using fair value adjustment. Here we will not talk about the fair value adjustment and how that should be countered in the treatment of the equity, because that is about how to negate the accounting disadvantage. Here we will focus on the tax disadvantage only.

Mark-to-market adjusted transactions are very much connected to the use of SPV's (Special Purpose Vehicles) in low- or no-tax jurisdictions. In order to secure a tax arbitrage using mark-to-market, a company has to establish ownership outside of a country and connect the pricing of the resulting transactions (rent or otherwise) to a market which fluctuates. To avoid the consequences of this way of organizing their operations, countries can start using a mechanism whereby deduction for mark-to-market cost transactions in-country is done at the same tax rate as the multinational company according to their public financial statements has achieved worldwide. PWYP Norway has chosen to call this mechanism reverse tax credit, as it uses the same principle that for a long time has been used to avoid double taxation of revenues. Instead, the tax credit principle is reversed, so that the deduction of cost is done at the same rate as the opposite revenues has been tax internationally. It has been demonstrated through extensive calculations that replacing the actual deduction of cost with a "tax credit" type calculated using the multinationals average tax rate, returns the taxation to what it would

[2] See "Protection Against Derivative Abuse", PWYP Norway 2011, https://www.publishwhatyoupay.no/sites/all/files/1006a-PWYP_DerivativesReport_ENG_DOWNLOAD_1.pdf

have been if the multinational company did not have low- or no-tax jurisdictions in their organization structure, i.e. as if there were no intrusive elements in the value chain. Using this method is very precise as it only targets the internal, cross-border cost transactions presented by the multinational company's in-country subsidiary in their tax return, as it is principle-based (only one rule for all companies) and as it is fair (a company is returned the tax rate it has tried to achieve globally for tax deduction purposes of internal, cross-border transactions). A multinational company not using low- or no-tax jurisdictions would have a higher tax rate, and would thus not be affected in most countries introducing such a mechanism because the global tax rate would be on par with or higher than most countries tax rate. There is no need to change international treaties as this mechanism is only intended for use on the taxation of the internal, cross-border transactions presented by the subsidiary in-country in their tax country and thus does not create taxation issues towards other countries.[3]

<u>Non-transactional cash flows</u>

Non-transactional cash flows are typically financial flows that do not have an individual sales contract or sales order behind it. Typical examples are royalties, overheads, marketing fees, procurement fees, logistics fees, technical fees, management fees etc. All of these are characterized by that there is a push of cost from headquarters/affiliated companies to the individual subsidiary in order to take on and deduct for tax purposes these costs in the tax return presented to each country's tax administration, and the subsidiary is not allowed to avoid these costs through using external alternatives. There thus exist a monopoly provider of these services and the valuation and pricing of these are incredibly difficult for any tax administration. The counter-mechanism is again Reverse Tax Credit, i.e. to present the subsidiary that presents such cost for tax deduction purposes with a mechanism whereby the tax rate allowed for these transactions in-country are equivalent to the tax rate that the multinational corporation has purposefully achieved worldwide outside the country in question.[4]

<u>Tax regulation transactions</u>

These transactions, that either by internal tax law or international tax treaties, are identified as transactions that are particularly regulated with respect to the taxation of the revenues in order to avoid double-taxation. However, there is no regulation of the opposite, where these transactions are presented as cost deductions in high-tax countries while the opposite revenue transactions often go to low- or no-tax jurisdictions. Examples of these transactions are interest, insurance, some type of royalties etc. The cost deductions in-country for these transactions needs to be adapted to how the countries have solved the revenue-side. However,

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[3] For more information on Mark-to-Market transactions and fair value adjustments, see "The Roller-Coaster Mechanism in the World Economy – Mark-to-Market and Transactions Outside the Market", PWYP Norway 2017, https://www.publishwhatyoupay.no/sites/all/files/Les%20rapporten%20på%20engelsk_0.pdf

For more information on Reverse Tax Credit, see "Taking Away the Tax Effect of Tax Havens – Cross Border Taxation Methods and Reverse Tax Credit", PWYP Norway 2017, https://www.publishwhatyoupay.no/sites/all/files/Les%20rapporten%20på%20engelsk.pdf

[4] Again, for more information on Reverse Tax Credit, see "Taking Away the Tax Effect of Tax Havens – Cross Border Taxation Methods and Reverse Tax Credit", PWYP Norway 2017, https://www.publishwhatyoupay.no/sites/all/files/Les%20rapporten%20på%20engelsk.pdf

if there is no solution on the revenue side, i.e. the revenue transactions are handled fully on the receiving end with no taxation of the revenues, the situation becomes the same for these transactions as for the non-transactional cash flows discussed above. The solution is the same - that the subsidiary that presents such cost for tax deduction purposes is presented with a mechanism whereby the tax rate allowed for tax deduction purposes for these transactions in-country are equivalent to the tax rate that the multinational corporation has purposefully achieved worldwide outside the country in question.[4]

Internal, cross-border transactions

Internal, cross-border transactions are the regular internal transactions which is the archetype of transfer pricing. These are typically contractually regulated such that there is a sales order behind each volume of the products or services that crosses the border and create a cost deduction internally in the subsidiary in-country. It is the same thing here as with the other internal cross-border transactions that the opposite revenue transactions are often found in either low- or no-tax jurisdictions or in pass-through jurisdictions on the way to a low- or no-tax jurisdiction. This creates a tax arbitrage on the transaction which give multinational companies a competitive edge over national companies. Introducing reverse tax credit, i.e. tax deduction based on the tax rate purpose-fully achieved by the multinational company globally excluding the country in question, is the best way to remove the tax arbitrage and re-establish fair competition.[4] It is important that the internal, cross-border transactions are not allowed to create a loss in-country before the reverse tax credit mechanism is applied. Internal, cross-border transactions should thus only be accepted for deduction that give raise to loss-carryforwards to the extent that they, together with other cost, does not create losses in more than the first 18 months upon start-up in a country.

Re-directed income – digitalized sales version 1

Re-directed income is where sales from an in-country delivery is paid to a receiver outside of the country. This is the case of AirBnB, Uber and other companies or networks that deliver products or services from a place in-country, but the payment goes out of the country. In this situation, there is a competitive disadvantage if these transactions are not taxed on par with comparable transactions provided by in-country companies or networks that both deliver and get paid for the services in-country. The only difference between these transactions are whether the payment is in-country or goes to a receiving party outside of the country. The solution to these transactions is that they need to have the same taxes levied on them no matter where the payment goes.

With VAT it is easy – if there is VAT on the payment if there is an in-country receiver of money for the product or service, then there should also be VAT on the payment that goes out of the country. As it is the end-user that pays the VAT, the only logical thing is to create, in todays digital world, a regulation that ensures that whenever a payment goes abroad for such goods or services, the debet card company (the bank) or the credit card company applies the VAT rate on the transaction amount and withdraws the amount from the debet or credit card and pays it directly to the tax authorities/ the treasury. The VAT arbitrage is thus alleviated, and the two transactions, one being paid in-country and the other being paid to an abroad receiver, becomes more equal and the competitive disadvantage for the national company become less.

There is still the problem with the corporate taxes that the national companies pay, though. In order for a national transaction to be competitive with a re-directed income transaction (delivery in-country, payment abroad) there must in addition to VAT be added a taxation to the re-directed income taxation that emulates the corporate tax that the national company pays. Only when the international transactions add this corporate tax emulation plus the VAT are the transactions paid in-country versus outside the country competitively comparable. The emulated corporate tax is comparable to a withholding tax with the only difference that it is paid by the customer and not the company as a normal withholding tax would be.

In the report "Taking Away the Tax Effect of Tax Havens – Cross Border Taxation Methods and Reverse Tax Credit" such taxation using VAT and withholding tax paid by the customer is described in more detail (in addition to the reverse tax credit method for in-country subsidiaries of multinational companies).[4]

<u>Cross-border Business-To-Customer (B2C) sales – digitalized sales version 2</u>
VAT and withholding tax paid by the customer in order to increase the transaction value of the international transaction up to the same level as the national transaction is also the best method to deal with cross-border transactions directly from an international company to individual customers in-country. The main purpose of the taxation is not the taxation per se, but to secure that the international transaction is not discriminating against the national transaction through the tax arbitrage that is only available for the multinational company in the international transaction.

The reason for why the VAT and the withholding tax is to be paid by the customer in B2C sales is two-fold:

- The most basic source for taxation is the purchasing power by customers. This can be taxed at various stages: when earned (income), when used (purchases) or when saved or invested (value). In ordinary transactions it is the national company that is pass-through to the tax authorities/the treasury for payment of VAT and it is the national company that pays the corporate tax on their taxable profit. However, the reason for this is that internally in a country, this seems like an efficient way of paying taxes. The high number of companies outside of the country paired with the fact that there may be quite a low number of transactions with most of the companies (and quite a high number of transactions with a few companies) means that it is more efficient and precise to make the customer directly responsible for paying the VAT and the withholding tax directly to the tax authorities than having these taxes paid by the international corporation. In a digital economy it is possible to pass legislation that secures that VAT and withholding tax is covered by the same payment solution as the transaction is paid by. If the VAT and withholding" tax is drawn from a debet or a credit card, then the same debet or credit card is used to pay the taxes directly to the tax authorities/the treasury.
- Another reason for having the customer pay the VAT and the withholding tax is that doing it that way does not directly interfere with the multinational company's pricing (it may indirectly affect the pricing), i.e. the multinational company does not have to change their price unless they want to. This is important, as different countries have different VAT-rates and would also possibly have different withholding tax rates. In order to secure that the multinational companies does not have to change their prices differently for different countries, it is important that it is the customer in-country that

faces the same price whether buying the goods or services in-country compared to buying it abroad. The main thing is to make transactions with national companies competitive with transactions the customer have with international companies. The customers choice should therefore be unaffected by any tax arbitrage. The country is indifferent as it gets approximately the same taxation whether the customer choose to buy from national or international companies.

B2C sales from abroad can thus be met with the same counter-mechanism of VAT and withholding tax as was explained for re-directed income. Whether the delivery in the digital sale is in-country or from abroad is therefore of no consequence. The important mechanism is to have the customer pay the VAT and the withholding at the same time as the transaction is being paid. Doing it this way ensures:

- That the taxes are tailored to the individual transaction and therefore always correct
- The VAT applied is the relevant for the country of the customer
- The withholding tax rate can be tailored to corporate tax level of the country of the customer
- That it is possible to automate the tax payments as all payments from individual customers to businesses abroad
- It is possible to exempt automatically payments for goods and services that has to be consumed abroad, such as air flights, hotels and restaurants and items bought abroad while on travel.[4]

3. Input to the OECD Task Force on the Digital Economy

In the introduction (item 1) to the Public Consultation Document it is said: "The Action 1 Report recognised that digitalisation and some of the business models that it facilitates present important challenges for international taxation. The report also acknowledged that it would be difficult, if not impossible, to 'ring-fence' the digital economy from the rest of the economy for tax purposes because of the increasingly pervasive nature of digitalisation."

PWYP Norway Comment: The challenges are greatest if one does not create a sub-typology of the various types of tax leakages. As demonstrated in section 2 above, creating such a sub-typology makes it easier to identify which remediating actions can be taken against various types of tax leakages, including those arising from digitalization. There is also no reason for ring-fencing as it is possible to target the individual digital transactions with VAT and withholding tax paid by the customer in order to secure that the total transaction value a customer face from national companies and multinational companies are approximately the same, and as both transactions create approximately the same taxes there is no major tax leakage anymore.

In section 1.1. The Interim Report (item 3) to the Public Consultation Document it is said: "In addition, several highly digitalised MNE groups have also changed their distribution models, which were based on remote sales, to local "buy-sell" distributors in response to the work on BEPS Action 7. In connection with the remaining BEPS challenges, some countries highlighted the risks that even after such a restructuring digitalised MNE groups would be able to use local limited risk distributors to justify only minimal tax in the market jurisdiction, while being able to shift a disproportionately high amount of profit to a small number of affiliates in remote locations provided there is a correlation with a certain level of physical activity (e.g. functions that control risks and functions relating to the development, enhancement, maintenance, protection and exploitation of intangibles (DEMPE)).”

PWYP Norway Comment: If all the three mechanisms suggested by PWYP Norway is enacted, it does not matter anymore whether multinational companies are selling using a B2C-model, re-directed income from a local presence or a full-scale subsidiary. If these mechanisms are enacted, it does not matter anymore how the multinational company organizes itself as the multinational company faces the relevant counter-mechanism that ensures that they stay competitive with national companies however they organize themselves, but they do not enjoy a competitive edge anymore due to the tax arbitrage that they previously enjoyed.

In section 1.1. The Interim Report (item 5) to the Public Consultation Document it is said: “In this context, the members of the Inclusive Framework committed to continue working together towards a consensus-based solution with the goal of producing a final report in 2020, with an update to the G20 in 2019. The work would therefore need to focus on the two outstanding issues posed by a rapidly digitalising economy: ongoing work on remaining BEPS challenges as well as a coherent and concurrent review of the nexus and profit allocation rules, including an exploration of the feasibility of different technical solutions that are consistent with the principle of aligning profits with underlying economic activities and value creation.”

PWYP Norway Comment: It is important to emphasize that PWYP Norway’s approach to the tax leakage issues is a coherent approach to the entire typology of tax leakages, not only digitalization. Digitalization, and evasive actions related to digitalization, is however adequately met by PWYP Norway’s coherent approach, and there are no other measures needed as all the different types of tax leakages are covered if all three mechanisms are enacted. It is impossible to include all the aspects of PWYP Norway’s coherent approach in this comment letter, but we encourage OECD to (1) review the reports that we have cited above and that are downloadable from PWYP Norway’s website www.pwyp.no and (2) to engage with PWYP Norway if there are items that are surfacing during the process where it is suggested that PWYP Norway’s approach does not fully cover the identified challenges. In such cases, it is highly likely that the approach covers the identified challenged, but that this has not been emphasized in the downloadable reports as the research has continued after the publications of the reports. Many questions that has been posed after the publication of the reports has been answered individually or collectively and has only strengthened the completeness of PWYP Norway’s approach. A very important aspect of PWYP Norway’s approach is that no profit allocation is needed, as all three mechanisms are directly targeting transactions that are in-country already (derivatives or internal, cross-border cost transactions presented for tax deduction in a tax return by a subsidiary) or are transactions or payments going abroad. Moving derivatives into a separate tax base does not pose any challenges with respect to calibrating the tax system. Returning a multinational corporation the tax rate they have achieved globally for tax deduction purposes in-country do not pose any challenges with respect to calibrating the tax system. Applying the same VAT-rate to international transactions as are applied to national transactions do not pose any challenges *to calibrating the tax system. The only calibrating needed is to find the applicable withholding tax rate a customer has to pay in order to secure that national and international transactions are competitively comparable. Countries should calibrate the withholding tax to ensure that national and international companies are competing on the same level, not maximizing taxes from multinational transactions.*

PWYP Norway's comments to the remaining Public Consultation Document:

- PWYP Norway is of the opinion that an approach addressing the three mechanisms identified by PWYP Norway is highly targeted, surgically precise and non-invasive towards other countries tax base as these three mechanisms only targets items that are already in-country (derivatives) or are crossing the border with a resulting payment which can be targeted directly (either for tax deduction purposes or for taxation purposes (VAT and withholding tax paid by the customer (drawn from the same account or credit as the transaction is paid from)).
- OECD's approach which includes profit allocation are bound to be invasive on (other) countries tax base and is therefore bound to be full of conflicts and need for ongoing negotiations and adjustments in order to try to improve the approach over time. As each corporation is different and each country's approach to tax is different it is difficult to see how one is to get to a principle-based taxation that is as targeted, precise and non-invasive as the three mechanisms that PWYP Norway has suggested.
- In item 52 is an excellent example of how the profit allocation is bound to initiate problems. The approach is dependent on:
    - the definition of the tax base to be divided > this means massive interpretation issues,
    - the determination of the allocation keys to divide that tax base > this means massive issues in defining the correct allocation keys, a task that is close to impossible as all companies are different,
    - the weighting of these allocation keys > this means massive issues in defining the correct weights, a task that is close to impossible as all countries have different approaches to taxation.
- Item 65 give an excellent example that the issues are identified, but the approach is not targeted enough: "65. … by failing to acknowledge the reality that businesses can today have an active presence or participation in market countries without a physical presence, or one that would justify a substantial allocation of income to that jurisdiction, the existing international tax rules fail to properly allocate income to the locations in which an enterprise is understood to create value in today's increasingly digitalised world." Here the Public Consultation Document equalize "presence or participation in a market … without a physical presence" with a taxation that "justify a substantial allocation of income to that jurisdiction". PWYP Norway will, referring to our arguments above, argue for that there are more targeted and precise mechanisms available than those OECD are forwarding. These mechanisms, unlike those promoted by the OECD, create few or no issues in the distribution of taxes between countries as they are all targeted towards items in-country or transactions or payments crossing a border.
- In item 80, the Public Consultation Document envisage "some changes to treaty provisions". PWYP Norway would emphasize that the three mechanisms that PWYP Norway promote does not envisage any changes to treaty provisions as all three

mechanisms is done in each country's internal tax legislation targeting transactions presented for tax deduction or out-bound payments crossing the border.
- In item 81, the Public Consultation Document envisage a "need to incorporate strong dispute prevention and resolution components". PWYP Norway would emphasize that the three mechanisms that PWYP Norway promote do not envisage any need for strong dispute prevention and resolution components as all three mechanisms is done in each country's internal tax legislation.

Based on the above, here are PWYP Norway's comments to the Public Consultation Documents questions in item 87:

1. What is your general view on those proposals? In answering this question please consider the objectives, policy rationale, and economic and behavioural implications.

   PWYP Norway comments: There are easier, more targeted and more precise ways of dealing with tax challenges from both digitalized businesses and general tax leakages as demonstrated by the three mechanisms that PWYP Norway promote. PWYP Norway's suggested approach is a coherent system that takes care of all tax leakages as demonstrated by the sub-typology that the mechanisms address. These and other approaches should be investigated before trying such a complicated and invasive system as the Public Consultation Document suggest.

2. To what extent do you think that businesses are able, as a result of the digitalisation of the economy, to have an active presence or participation in that jurisdiction that is not recognised by the current profit allocation and nexus rules? In answering this question, please consider:
   i. To what types of businesses do you think this is applicable, and how might that assessment change over time?

   PWYP Norway comment: Digitalisation of the economy will of course pose challenges to the existing tax system, but it is possible to address these challenges through much more direct and targeted approaches that those suggested in the Public Consultation Document, as evidenced by the three counter-mechanisms suggested by PWYP Norway above.

   ii. What are the merits of using a residual profit split method, a fractional apportionment method, or other method to allocate income in respect of such activities?

   PWYP Norway comment: It is our opinion that there are no merits in using any method that is based on profit split methods, apportionment methods or other methods to *allocate* income for taxation purposes. As demonstrated above, in the description of the three counter-mechanisms that is possible to use, there is no need to *allocate* revenues, costs or profits as long as one can use principle-based methods to target precisely the various types of tax leakages that is occurring (ref the sub-typology). Allocation means two undesirable things: (1) estimation and (2) many countries involved.

3. What would be the most important design considerations in developing new profit allocation and nexus rules consistent with the proposals described above, including

with respect to scope, thresholds, the treatment of losses, and the factors to be used in connection with profit allocation methods?

PWYP Norway comment: It is desirable to avoid any system of profit allocation as long as there are mechanisms available to address the problems directly, as demonstrated by the three mechanisms suggested by PWYP Norway. This direct approach which targets the transactions directly and surgically correct is much more desirable both to countries (that do not risk invasive mechanisms into their tax base) and to companies (that do not risk highly complicated tax systems applied to their profit base).

4. What could be the best approaches to reduce complexity, ensure early tax certainty and to avoid or resolve multi-jurisdictional disputes?

   PWYP Norway comment: To reduce complexity – move derivatives into a separate tax base. To ensure tax certainty and to avoid multi-jurisdictional disputes – apply the tax rate achieved by the multinational company globally to the tax deduction for the subsidiary in-country for internal, cross-border cost transactions claimed for tax deduction in the tax return, and use VAT and withholding tax paid by the customer on digitalized transactions cross-border, whether these are re-directed income or internationally originated B2C sales.

4. Input on the Global anti-base erosion proposal

In section 3 Global anti-base erosion proposal, the Public Consultation Document promotes an income-inclusion rule and a tax on base eroding payments. These suggestions are closer to what PWYP Norway has suggested, and PWYP Norway would encourage OECD TFDE to look into PWYP Norway's suggestion as applicable mechanisms that is already addressing a relevant sub-typology with respect to tax leakages (not only from digitalization).

The inherent issues with the Public Consultant Documents proposals are:
- an ***income inclusion rule*** that would tax the income of a foreign branch or a controlled entity if that income was subject to a low effective tax rate in the jurisdiction of establishment or residence;

PWYP Norway comment: taxing the transactions going cross-border is much more precise than making international companies taxable to all countries they have a marketing or sales presence in which seems to be the implication of an income inclusion rule.

- a ***tax on base eroding payments*** that would deny a deduction or treaty relief for certain payments unless that payment was subject to an effective tax rate at or above a minimum rate.

PWYP Norway comment: one of PWYP Norway suggestions reduce the deduction for internal, cross-border cost transactions down to the tax rate that the multinational company has purposefully achieved worldwide as demonstrated through the tax rate in the global financial statement. This seems a more principle-based approach than accepting/denying deductions based on whether or not a payment has been subject to an effective tax rate at or above a minimum rate.

The third issue is that in addition to an income inclusion rule, there is need for an income exclusion rule with respect to derivatives in order that speculative use of derivatives cannot influence the tax base of the general tax income in a business.

The most beneficial results of implementing the PWYP Norway suggestions are:

- Moving derivatives and derivative-like contracts into a separate tax base means that a whole class of transactions that complicate business tax returns tremendously are completely removed from the general tax return. This means that it does not matter how many more derivatives are being created in the future – they will always have to be presented in a separate tax base separated from the general taxable profit. This will simplify the tax administrations control of business income significantly as well as it almost removes the need for controlling the derivative tax base as this tax base will only result in any taxation should derivative profits supersede derivative losses and as derivative losses cannot be carried forward against other taxable revenues than future derivative profits. PWYP Norway's suggestion to move derivatives into a separate tax base is thus a tremendous simplification for tax administrations. The proposal does not prohibit companies from using derivatives for hedging purposes and it does not prohibit companies from doing speculative trading in derivatives in the same country either. It only discourages companies from speculative trading in derivatives where it is possible to place losses in high-tax jurisdictions while the opposite derivative profits are placed in low- or no-tax jurisdictions.
- Giving back the global tax rate of a multinational corporation as the tax rate for deduction of internal, cross-border transactions is a universal method, as any new types of cross-border transactions will fall under the same regulation. This means that this type of regulation is robust and it clearly identifies all transactions to include (internal and cross-border) without further need for definition. If implemented by all countries, simulations show that the taxation of the corporation is returned to the tax level the company would have had if the corporation did not have any intrusive elements (no low- or no-tax jurisdictions) in its value chain. It also means that corporations that do not use low- or no-tax jurisdictions will automatically get higher deductions, and it also means that corporations tax situation will improve steadily as it reduces the use of low- or no-tax jurisdictions without any need for changing the regulation. This demonstrates that this type of regulation is also robust and targeted.
- As VAT and withholding tax paid by the customer allows for a principle-based and targeted approach to digitalised business models, this type of regulation does not need to change as digitalised business models changes. Any type of payment, except for those for consumption in other countries (flights, hotels, restaurants etc), going from individual customers to businesses abroad would result in VAT and withholding tax being withdrawn from the debet or credit card. Any other payment method could be solved by VAT and withholding tax being prepaid and the tax payment receipt being provided before the other payment method (for example invoice) would be allowed.

Based on the above, here are PWYP Norway's comments to the Public Consultation Documents questions in item 110:

Commentators views are requested on the policy, technical and administrability issues raised by the proposals described above, including those raised in paragraphs 100 and 105.

PWYP Norway comment: The sub-typology and the counter-mechanisms PWYP Norway has developed go along way to provide guidance to the issues raised in paragraphs 100 and 105.

In particular, comments are specifically requested on the questions set forth below:

1. What is your general view on this proposal? In answering this question please consider the objectives, policy rationales, and economic and behavioural implications of the proposal.

PWYP Norway comment: PWYP Norway believe the OECD is closer to the right thinking in this section, but we still believe that the OECD would benefit tremendously, not only in the digitalized area, by reviewing the suggestions PWYP Norway has promoted as these has undergone extensive research and/or simulations demonstrating that these are highly efficient and highly targeted mechanisms immediately applicable.

2. What would be the most important design considerations in developing an inclusion rule and a tax on base eroding payments? In your response please comment separately on the undertaxed payments and subject to tax proposals and also cover practical, administrative and compliance issues.

PWYP Norway comment: We believe our above comments have adequately covered the design considerations needed. The mechanisms need to be highly efficient, highly targeted, robust and with no need for future changes. This means that the mechanisms implemented needs to include whole classes of transactions that makes for these mechanisms not needing further changes although the classes included expands through more available instruments. This is how PWYP Norway has designed the three mechanisms that is available for closing almost all the tax leakages that is currently in existence.

3. What, if any, scope limitations should be considered in connection with the proposal set out above?

PWYP Norway comment: No comment as introducing the three mechanisms suggested by PWYP Norway would address all current tax leakages in the current sub-typology as described above.

4. How would you suggest that the rules should best be co-ordinated?

PWYP Norway comment: Co-ordination of the implementing the three mechanisms suggested by PWYP Norway would mainly involve recommendations, as all other implementations would be in the internal tax law in the different countries. We do not recommend going down a road which involves a lot of co-ordination. Regulations in need of a lot of co-ordination indicates ineffective and non-targeted regulations.

5. What could be the best approaches to reduce complexity, ensure early tax certainty and to avoid or resolve multi-jurisdictional disputes?

PWYP Norway comment: The best suggestion we have is to review and recommend the coherent approach that PWYP Norway suggests, as these are simply to implement and use but highly efficient and highly targeted towards the goals OECD is working towards.

5. Recommendations

PWYP Norway would encourage the TFDE to review PWYP Norway's comments and suggestions in view of the proposals, questions and suggestions provided in the Public Consultation Document.

As PWYP Norway's suggestions are thoroughly researched and through simulations have been shown to be robust and targeted without any need for complicated systems for allocation, follow-up of adaptations and dispute mechanisms between countries and between country and companies.

Yours sincerely

Mona Thowsen

Secretary General

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