

Pillar One: Amount B

Headlines and initial observations

On 8 December 2022, the OECD released a public consultation document titled “Pillar One – Amount B”. The document builds on the commitment the OECD/G20 Inclusive Framework on BEPS (“IF”) reached in October 2021, to simplify and streamline the application of the arm’s length principle to in-country baseline marketing and distribution activities.

Amount B is designed to address the challenges low-capacity jurisdictions face applying transfer pricing rules, help re-stabilize the international tax system, and reduce the compliance costs businesses incur due to transfer pricing disputes. This document provides the first detailed insights into how the IF considers Amount B could operate, since the Pillar One Blueprint was published more than two years ago.

The public consultation on Amount B runs through January 25, 2023. While technical work on Amount B will no doubt continue, interested parties should consider submitting comments during the consultation period.

Consultation Document

Amount B is a core component of Pillar One of the OECD’s two-pillar solution addressing the tax challenges arising from the digitalization of the economy, though critically is not limited to digital businesses.

The document identifies its objective as simplifying and streamlining the application of the arm’s length principle based on the guidance provided in the OECD Transfer Pricing Guidelines. This emphasizes that in contrast to Amount A, Amount B is not intended to allocate more taxing rights to market jurisdictions. Nor is it intended that Amount B be limited to groups above a certain revenue or profitability threshold.

The document has four substantive sections:

1. **Scope of Amount B** discusses how “baseline marketing and distribution activities” would be defined using a set of qualitative and quantitative criteria.
2. **Amount B pricing methodology** outlines a pricing methodology that would apply to in-scope transactions.
3. **Documentation requirements** describes the documentation requirements that taxpayers would need to comply with when applying Amount B.

4. **Tax certainty** explains the design of a tax certainty framework that will be used to resolve disputes arising from the application or operation of Amount B.

The OECD's objective is to reach agreement on Amount B by mid-2023, allowing it to come into effect in 2024 alongside Amount A.

The rest of this summary covers these four sections in more detail.

Scope of Amount B

Amount B would apply to “buy-sell” arrangements where the tested party purchases goods from a related party for wholesale distribution to unrelated parties. Amount B may also apply to sales agency and commissionaire arrangements, though the document recognizes that seeking to cover these different types of arrangements may create challenges for establishing a standardized pricing methodology and specifically asks whether sales agents and commissionaires should be included in scope, noting that IF members have different views.

For simplicity, it is proposed that Amount B would apply to controlled transactions involving the distribution of tangible property, but not the distribution and marketing of services (including financial services) or digital property (such as software). The consultation asks for views on these exclusions.

The applicability of Amount B to distributors that meet those broad definitions would be determined using a number of scoping criteria, which are both qualitative and quantitative. For example, an in-scope distributor should not undertake valuable and material regulatory compliance activities; perform important technical or specialized services; own or generate unique and valuable intangible assets; or assume more than limited risks. Proposed quantitative indicators include limits on proportions of marketing and advertising expenses, packaging and assembly costs, and support services. The document requests feedback on these proposed criteria, where there are a number of open questions.

The document seeks views on whether an exemption from Amount B should apply where another transfer pricing method is the Most Appropriate Method (“MAM”) and/or where there are local market comparables (or comparables in another similar market). Given the arguments taxpayers already face around method selection and the existence of local market comparables, these exemptions are a potential cause for concern.

The document indicates that despite the introduction of Amount B, the terms of existing Advance Pricing Agreements (“APAs”) should be respected and that APAs will continue to play a role in delivering tax certainty. This is a welcome development, given the greater flexibility APAs provide to taxpayers and tax administrations to get tax certainty over complex and/or unique fact patterns.

Amount B pricing methodology

The proposed Amount B pricing methodology aligns with current transfer pricing practices. It is proposed that a benchmarking analysis would be performed based on a set of publicly available comparable financials.

The IF is exploring two outputs with similar underlying methodologies:

1. A **pricing matrix approach** setting out a range of profitability figures against two or more statistically significant quantitative measurements (for example, the ratios of asset intensity and operating expenses to sales); or
2. A **mechanical pricing tool** that would use an econometric model to translate the benchmarking data that would apply based on the financial data of the tested party.

In simple terms, the pricing matrix approach would establish a range of variables and a taxpayer would be responsible for establishing where they fall compared to subsets of the comparables grouped according to their economic characteristics. Under the mechanical pricing tool approach, a taxpayer would input the financial data of a tested party into the tool which would determine the Amount B return for that tested party based on a weighting of economic characteristics.

The consultation suggests that the Amount B return would generally be calculated using operating margin (net profit divided by sales) as the Net Profit Indicator (NPI),¹ though it holds open the possibility that the Berry Ratio (gross profit / operating expenses) or a combination of NPIs could be used.

The fact that some IF members recognize that it would not be appropriate to set the returns for all marketing and distribution activities using operating margin is likely to be a welcome development, as this is particularly important for companies that perform marketing and distribution activities that fall short of the baseline standard. However, the IF has not reached consensus on the use of alternative NPIs, making this an important area for comment.

Documentation

Rather than provide a simplified framework, the proposed documentation requirements retain and build upon the accepted master file / local file transfer pricing documentation standards set out in the OECD Transfer Pricing Guidelines.

The overriding objective is to ensure that tax administrations have sufficient information to inform the assessment of whether a taxpayer's controlled transactions are in-scope and hence can be priced using the Amount B pricing methodology. However, the extensive documentation requirements proposed in the consultation document exceed the OECD's recommend requirements for local files and request some items – such as a copy of any relevant bilateral APAs – that go well beyond what is generally expected in documentation. This is an issue that we expect will be raised by consultation respondents.

This section also discusses whether business could restructure to get into or out of scope of Amount B and suggests that the IF may adopt restrictions to limit access in some scenarios. This proposal runs counter to the recognition that businesses restructure for a variety of commercial reasons and in particular risks disadvantaging businesses that undergo restructuring to reduce the scale of marketing and distribution activities performed in markets.

Tax certainty

For taxpayers, a recurring concern is that the OECD will reach agreement on Amount B, but the benefits of this simplification will be curtailed because some tax administrations choose not to apply it – or that others may seek to apply it beyond its intended scope. The former risk is a challenge that has already arisen in respect of the OECD's work on low-value adding services. The document addresses these issues at a high level, outlining how the Mutual Agreement Procedure, and, potentially, existing treaty arbitration provisions, could be used to resolve disputes and eliminate any double taxation arising from the application of Amount B.

The tax certainty process is vital if Amount B is to apply successfully in practice, as well as in theory. It is unclear from what is being proposed whether IF members are sufficiently committed to putting in processes that would be necessary to provide businesses with real certainty.

How should businesses be responding?

Amount B has the potential to deliver significant benefits to both taxpayers and tax administrations, if scoped, priced and administered appropriately.

¹The NPI is equivalent to the Profit Level Indicator (PLI) under the U.S. transfer pricing regulations.

It is helpful to see how IF members envisage Amount B could operate. However, there are a variety of areas where improvements could be made, on which it is anticipated responses to the consultation will be focused.

Some key questions that businesses should consider when assessing the impact of Amount B are:

1. Would it be better if Amount B is broadly applicable or narrowly tailored? Would the proposed MAM and local comparables exceptions yield the right scope for Amount B?
2. Are the marketing and distribution activities performed by my business within the scope of Amount B? Is that outcome (either in-scope or out-of-scope) appropriate? Is the outcome clear, or could this be an area where disputes arise?
3. If the marketing and distribution activities of my business are in-scope, how should the Amount B pricing methodology be designed to deliver an appropriate outcome in an administrable fashion?
4. How onerous are the Amount B documentation requirements for my business? Will Amount B actually lower compliance costs when compared to current transfer pricing documentation requirements?
5. Will existing certainty mechanisms function appropriately ensure that my business has certainty over the application of Amount B and that tax administrations are not able to arbitrarily prevent my business from utilizing this simplification (or to apply Amount B where my business should be out of scope)?

OECD webinar

The OECD produced a [webinar](#) to accompany the release of the consultation document, which offers a good introduction to a complex document. In the webinar, the OECD Secretariat emphasized that Amount B is coming – and that the key question is how broad the scope will be.

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