SwissBanking

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Basel, 12 November 2019
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Public Consultation on the Secretariat Proposal for a "Unified Approach" under Pillar One

Dear Madam, Dear Sir,

The Swiss Bankers Association ("SBA") would like to thank you for the opportunity to provide comments on the proposal of the OECD Secretariat for a "Unified Approach" under Pillar One. The SBA is the voice of the banks in Switzerland. As an umbrella organisation, we represent almost all banks in Switzerland.

To begin with, we want to point out that the regime envisaged in the "Unified Approach" will have far-reaching consequences for all international companies, irrespective of whether they serve markets remotely or are highly digitalized or highly profitable. This significant collateral consequences should be taken into account when laying out the specifications of the regime. The impact of the new regime on companies and entire industries that are not primarily in scope of its policy objective must be kept at a minimum. Otherwise, the economic disruptions caused by the new regime are likely to outweigh potential gains for the markets jurisdictions.

The overall objective of this initiative must include a stable and certain environment for both taxpayers and tax administrations. This can only be achieved if the underlying principles of the entire framework are widely accepted by the various stakeholders involved. For this purpose, the specifications of the new regime should provide tax certainty and minimize the administrative burden.

Further, we would like to remind the Secretariat that the primary goal of the OECD initiative was to modernise current tax rules and to adapt them to an increasingly globalized and digitalized world economy. Consequently, the new regime must have a clear focus and target those industries and companies for which existing rules proved to be inadequate. This is the case for example for technology companies that scale their offerings by remotely reaching into markets unconstrained by physical presence. Other industries in essence still follow a rather traditional business model which, in the case of banking, is mostly connected to a physical presence in a market.

1. Carve-out for the banking industry

SBA fully supports the call of the international banking associations for a carve-out for the banking industry. Considering the specificities of the banking business – especially the strict regulatory framework banks operate within and the significant restrictions in "reaching into" foreign markets – banks generally pay their fair share of taxes in the countries where they operate and thus should simply not be the primary concern of this OECD initiative.

For further elaborations on why banks should be carved out, we refer to the comments that the ***International Banking Federation (IBFed)*** submitted as part of this consultation process complementing previous IBFed statements and exchanges with the Secretariat.

2. Overall assessment of the "Unified Approach"

SBA is deeply concerned about the overall consequences of the OECD proposal on the Swiss economy and international companies. We therefore endorse the comments of ***economiesuisse and SwissHoldings***, the two main umbrella organizations of Swiss businesses.

3. General comments on the "Unified Approach" proposal

Even though we fully support IBFed's demand for a carve-out for banks, we take the liberty to elaborate further on a number of considerations that are specifically important for SBA in addition to the comments of economiesuisse and SwissHoldings.

Please see our comments below, starting with some general comments that are followed by the SBA's input on the specific questions raised in the consultation document in the Appendix:

a) Harmonization/standardization of requirements

The regime established by the OECD will have to be implemented into local laws across the global economy. This will create an enormously complex system for all companies operating in multiple jurisdictions. In order to alleviate the disruption caused by the new regime and to avoid double taxation, it is absolutely vital that the standards are implemented in a harmonized manner, both from a content and timing perspective. Fragmentation, disharmonized rules and administrative burdens must be avoided or kept to a minimum and implementation and maintenance costs of the new regime must be minimized by relying on a standardized framework. For this purpose, jurisdictions' leeway to deviate from the standard must be strictly limited.

b) Centralized approach for operationalization

Administering the regime as envisioned under the “Unified Approach” will be extremely onerous for all in-scope companies. In particular, the costs and risks of both the implementation and the maintenance of the new regime are of great concern.

In order to alleviate the disruption, we suggest a centralized approach for the operationalization of the regime. The tax administration of the jurisdiction where the head office of the corporation is located should play a key role. This tax administration should act as the single point of contact and collect the information that is necessary for the administration of the regime, collect tax revenues, reallocate and distribute the portion of tax revenue that is assigned to each eligible market jurisdiction.

With this setup, administration would be consolidated at the head office level of in-scope corporations. The local tax administration would be in charge of administering the regime and the exchange of information and tax revenue would take place through official channels. Corporations would need to adhere to the requirements of the new regime based on their obligations towards their local tax administration, which would ensure a level playing field.

c) Dependent agent

The existing concept of the dependent agent permanent establishment under the OECD Model Tax Convention becomes obsolete with the new regime. The dependent agent concept envisages to cover activities where a person acting on behalf of an enterprise in a market jurisdiction and, in doing so, habitually concludes contracts or plays the principle role leading to the conclusion of contracts. In order to avoid distorting overlaps with the new nexus definition which also envisages to cover the interaction with clients in a market jurisdiction, the dependent agent concept must be eliminated when incorporating the new regime into the OECD Model Tax Convention.

d) General de minimis threshold

The new regime based on the “Unified Approach” risks creating economic burdens that outweigh the potential benefits expected for market jurisdictions. In order to limit the “noise” and create adequate focus of the regime, its scope should be limited to the most relevant companies and the most relevant markets.

This could be achieved by implementing specifics thresholds. On the one hand, companies whose relevant (i.e. cross-border) revenue is not very substantial on a group level should be excluded. On the other hand, a simple de minimis threshold of USD 1 revenue per inhabitant of a country could be applied to in-scope companies. Hence, the regime would only apply to companies that have a revenue of USD 1 or more per inhabitant of a given market. This proportionate threshold would limit the scope of the regime to companies and markets where substantial gains can be expected and at the same time allow flexibility for smaller economies to also benefit from the redistribution of profits envisaged under the new regime.

e) Open questions

SBA wants to point the attention to some key questions that remain unanswered in the current proposal document:

- **Impact assessment:** What is the potential outcome and expected cost of the initiative? We believe that jurisdictions need to know what impact a new regime will have on their tax base. Accordingly, the key drivers for the redistribution of the tax base must be known. Without being able to adequately assess the effects, the technical elements of the approach can only be evaluated to a very limited extent.
- **Enforcement**: How will the new rules be enforced at the level of taxpayers and tax administrations? Will conflict resolution and arbitration rules be sufficiently robust and effective to ensure a level playing field and to avoid double taxation?
- **Volatility:** The global economy is highly volatile. How can scope and new nexus of the regime be designed to cope with this volatility, e.g. regarding the monitoring of thresholds over time and whether they should apply yearly or over a period of time?
- **Excess profit:** How can a one-size-fits-all approach sufficiently differentiate what a "normal" profit is, given the tremendous variety of average profitability among different industries? The residual portion of a profit depends heavily on the specificities of a particular industry.
- **Losses:** How will the new profit allocation rule be applied if an MNE is in an overall loss situation? How will prior year losses (tax losses carried forward) be recognized? If they were to be recognized, how would prior year losses be taken into consideration if the allocation key was different between different years?

f) SBA's answers to the questions raised in the consultation document

Please see separate Appendix.

We thank you for taking due consideration of our comments.

Yours sincerely,
Swiss Bankers Association

J. B—ikolz

Petrit Ismajli	Jean Brunisholz
Head of Tax Department	Head Swiss Tax

Appendix to Cover Letter

Swissbanking (SBA) Comments on the Secretariat Proposal for a "Unified Approach" under Pillar One

ISSUE	QUESTION	SUB-PART	COMMENTS
1. Scope	Under the proposed “Unified Approach”, Amount A would focus on, broadly, large consumer (including user) facing businesses. What challenges and opportunities do you see in defining and identifying the businesses in scope, in particular with respect to:	a. their interaction with consumers/ users?	Customers of banks can be individuals or entities. Therefore, for purposes of the new regime, the contracting party of a bank should be considered the relevant customer/user.
		b. defining the MNE group?	The definition of an MNE group should rely on the obligation to consolidate according to the relevant accounting standards (i.e. IFRS, US GAAP and/or local legislation of headquarter jurisdiction). It is important to note that all group entities of an MNE group must be treated equally for purposes of the new regime. Otherwise, complexity would make the regime unmanageable. As a general point, any new regime should, where possible, be clearly linked to recognized economic and tax policy principles without making significant changes to how current rules work regarding traditional taxing rights in jurisdictions involving physical presence.
		c. covering different business models (including multi-sided business models) and sales to intermediaries?	Due to the unique characteristics of the banking business, it is often impossible to distinguish business-to-business activities from business-to-customer services provision. For example, a bank can service a client directly or through an external asset manager. There is a substantial risk that setting up rules trying to distinguish one type of service provision from the other would make the new regime more complex without providing sufficient clarity for banks and other MNEs on what is in scope.

			In order to ensure equal treatment of all industries and business models, the new regime should not distinguish between different types of recipients of an entity's goods or services but instead generally treat the contracting party as the relevant customer/user. **Overall, the framework proposed under the new regime is not compatible with the defining characteristics of the banking business. This is a reason why IBFed argues for a carve-out of the banking industry.**
		d. the size of the MNE group, taking account of fairness, administration and compliance cost?	The main aim of the new regime as envisaged under the "Unified Approach" is to target the largest, most technologically advanced and most profitable international businesses with multiple billions of global revenues. Further, the relevant revenue ought to be significantly derived from remotely servicing clients in a market where the company has no physical presence, typically with a business model that heavily scales innovation towards mass markets. In order to be effective and to prevent implementation costs from outweighing potential gains, the new regime should strictly focus on MNEs with these characteristics, i.e. the largest and most global MNEs. There is a general aim to rely on existing concepts for purposes of defining a de minimis threshold. However, the EUR 750 million revenue threshold used for country-by-country reporting falls short of the overall purpose of the regime because too many companies would be in scope that do not meet the above-mentioned criteria. The threshold should be considerably higher to focus on relevant MNEs. In addition, it must be acknowledged that the domestic revenue of a company should be excluded from the calculation of an MNE group's profit as this part of the business clearly is not in scope of the new regime. For banks, certain activities such as for example treasury activities and proprietary trading are by nature a domestic activity and thus should be excluded.

			This would allow the exclusion of large but mainly domestically oriented MNEs where in any case no substantial profits could be reallocated to market jurisdictions that are insignificant for a particular company. Alternatively, or in addition, a certain percentage threshold for an MNE's international business could be implemented. For example, MNEs that do not generate the majority of their revenue abroad should not be in scope of the new regime. Finally, the new regime risks creating an economic burden that outweighs the potential benefits expected for market jurisdictions. In order to limit the "noise" and create adequate focus of the regime, its scope should be limited to the most relevant companies and the most relevant markets. This could be achieved by implementing a simple de minimis threshold of USD 1 revenue per inhabitant of a country. Hence, the regime should only apply to companies that have a revenue of USD 1 or more per inhabitant in a given market. This would limit the scope of the regime to companies and markets where substantial gains can be expected and at the same time allow flexibility for smaller economies to also benefit from the redistribution of profits envisaged under the new regime. **Banks simply do not generate substantial revenue that is in scope of the new regime. This is a reason why IBFed argues for a carve-out of the banking industry.**
		e. carve outs that might be formulated (e.g., for commodities)?	**SBA fully supports a comprehensive carve-out of the banking industry. We refer to the detailed comments of the International Banking Federation (IBFed) for this question**.
2. New Nexus	Under the proposed "Unified Approach", a new nexus would be developed not dependent on physical presence but largely based on sales. What challenges and opportunities do you see in defining and applying a new nexus, in particular with respect to:	a. defining and applying country specific sales thresholds; and	As a general point, the risk that monetary or activity-based thresholds create an unlevelled playing field as a result of countries' different sizes and tax administration approaches must be emphasized. Moreover, the new regime risks creating an economic burden that outweighs the potential benefits expected for market jurisdictions. As outlined above, the overall objective of the new regime is to focus on the largest, most technologically advanced and most

			profitable international businesses with multiple billions of global revenues. In order to limit the “noise” and create adequate focus of the regime, its scope should be limited to the most relevant companies and the most relevant markets. This could be achieved by implementing a simple de minimis threshold of USD 1 revenue per inhabitant of a country. Hence, the regime should only apply to companies that have a revenue of USD 1 or more per inhabitant in a given market. This would limit the scope of the regime to companies and markets where substantial gains can be expected and at the same time allow flexibility for smaller economies to also benefit from the redistribution of profits envisaged under the new regime. Further, it must be acknowledged that the revenue of a company in a given jurisdiction does not necessarily correlate to the profit earned in this market. A revenue threshold therefore is an inaccurate proxy for expected country-specific profits. This is an inherent flaw of the new regime envisaged under the “Unified Approach”. In addition, it must be ensured from an operational point of view that all countries have the same understanding of how to define revenue for purposes of the new regime (e.g. net or gross). Harmonization is absolutely key and no differentiation across jurisdictions should be permissible. With regard to the definition of the new nexus rules, only the home country of the MNE should be able to determine a new nexus in another country. If each country could determine whether a new nexus exists with regard to its market, this would create excessive legal uncertainty. Only the company’s head office and the local tax authority have the relevant information to make this determination (see our elaborations regarding a centralized approach). Moreover, it must be pointed out that the existing concept of the dependent agent under the OECD Model Tax Convention becomes obsolete with the new regime. The dependent agent concept envisages to cover activities where a person acting on behalf of an enterprise in a market jurisdiction and, in doing so, habitually concludes contracts or plays the principle role leading to the conclusion of

			contracts. In order to avoid distorting overlaps with the new nexus definition, which also envisages to cover the interaction with clients in a market jurisdiction, the dependent agent concept must be eliminated when incorporating the new regime into the Model Tax Convention. **Banks generally do not generate substantial revenue in markets where they are not physically present and licensed to operate. This is a reason why IBFed argues for a carve-out of the banking industry.**
		b. calibration to ensure that jurisdictions with smaller economies can also benefit?	Please see above our elaborations regarding the USD 1 per inhabitant revenue threshold providing flexibility to accommodate smaller economies.
3. Calculation of Group Profits for Amount A	The starting point for the determination of Amount A would be the identification of the MNE group's profits. The relevant measure could be derived from the consolidated financial statements. In your view, what challenges and opportunities arise from this approach? Please consider in particular:	a. what would be an appropriate metric for group profit?	Group profit should be determined by using Group GAAP (in line with IFRS, US GAAP etc.). The specific metric used should be earnings before tax (EBT). Some metrics such as for example EBITDA are not applicable for banks. As every company calculates EBT, referring to this metric ensures equal treatment of all industries. Further, it must be acknowledged that banking in particular is a highly volatile industry. Therefore, it is absolutely vital that the new regime factors in losses and tax losses carried-forward. This means that if there are no profits in a given year, nothing can be re-allocated and no tax revenue is to be expected in market jurisdictions for this year. As outlined above, the determination of the relevant group profit cannot be based on a one-size-fits-all approach. The domestic revenue of a company (including, for example, for banking the revenues from treasury activities and proprietary trading) should be excluded from the calculation of an MNE group's profit as this part of the business clearly is not in scope of the new regime. This would allow the exclusion of large but mainly domestically oriented MNEs where in any case no substantial profits could be reallocated to market jurisdictions. Alternatively, or in addition, a certain percentage threshold for an MNE's international business

			could be implemented. For example, MNEs that do not generate the majority of their revenue abroad should not be in scope of the new regime. **Banks are generally domestically oriented because they serve markets through locally licensed entities, i.e. subsidiaries or branches. This is a reason why IBFed argues for a carve-out of the banking industry.**
		b. what, if any, standardized adjustments would need to be made to adjust for different accounting standards?	In view of the already exuberant complexity of the new regime, no further adjustments should be made
		c. how can an approach to calculating group profits on the basis of operating segments based on business line best be designed? Should regional profitability also be considered?	Regarding segmentation, the new regime should adhere to already defined principles such as IFRS and/or other accounting standards (e.g. triggered by a decision-making body). In case segmentation applies, the relevant taxpayer would still need to be the "parent" entity (either business line or regional), in line with the centralized approach for operationalization. If existing accounting standards do not require segmentation, the overall profit of the entire group should be the relevant metric. Overall, MNEs need flexibility because a one-size-fits-all approach would fail to adequately meet the specific requirements of different industries.
4. Determination of Amount A	In determining Amount A, the second step would exclude deemed routine profits to identify deemed residual profits. The final step would allocate a portion of the deemed residual profits (Amount A) to market jurisdictions based on an agreed allocation key (such as sales). In your view, what challenges and opportunities arise from this approach?		It must be emphasized that for structural reasons, profitability varies largely across industries. Even within the same industry, big differences occur across business lines, regions and market segments. For banks, for example, retail banking offers significantly lower profit margins compared to other banking services such as discretionary asset management mandates. Moreover, profitability fluctuates substantially over time, in banking often correlating to the overall economic cycle. Therefore, one single number to separate "normal" profits from "excessive" profits would create substantial distortions and would fail to treat different industries equally. There are some banking-specific considerations regarding the definition of "excess profit". For banks, contrary for example to

			consumer goods companies, profits are only to a very small extent driven by brand value but rather by factors such as product innovation, superior portfolio allocation and investment decisions. These factors are directly tied to, for example, a skilled workforce and efficient processes. Moreover, banks employ a considerable amount of financial capital and financial risk which in turn plays a crucial role in generating a bank's profits. Consequently, for banks, only a very minor portion of the "deemed non-routine profit" is linked to marketing intangibles. According to a study of Copenhagen Economics[1], intangibles in banking only represent a modest share of the of total enterprise value compared to other sectors. The overall aim of the new regime is to capture highly mobile profits that under the current system are moved from one jurisdiction to another without any link to the market jurisdiction where the goods or services are sold. In particular, the aim is to capture businesses that generate excess profits, often by scaling innovation on a global scale. Contrary to that, banks' profits are primarily driven by tangible factors and thus the "deemed residual" portion that could be redistributed is infinitesimally small. **For banks, no substantial deemed residual profit would occur. This is a reason why IBFed argues for a carve-out of the banking industry.**
5. Elimination of Double Taxation in Relation to Amount A	What possible approaches do you see for eliminating double taxation in relation to Amount A, considering that the existing domestic and treaty provisions relieving double taxation apply to multinational enterprises on an individual-entity and individual-country basis? In particular, which challenges and opportunities do you see in:	a. identifying relevant taxpayer(s) entitled to relief?	Administering the regime as envisioned under the "Unified Approach" will be extremely onerous for all in-scope companies. In particular, the costs and risks of both the implementation and the maintenance of the new regime are of great concern. In general, the harmonization of the standards of the new regime is key. If jurisdictions have leeway, complexity would become unmanageable. In order to reduce complexity, the relevant entity could be the one "closest" to the marketing intangible, i.e. the functional owner of the brand. This would also correspond with current Transfer

[1] 19 February 2019, FUTURE TAXATION OF COMPANY PROFITS: WHAT TO DO WITH INTANGIBLES?, figure 1, p. 8 (https://www.copenhageneconomics.com/dyn/resources/Publication/publicationPDF/4/474/1550496379/future-taxation-of-company-profits_15022019_finalreport.pdf)

			Pricing rules which centre on the entities that are the functional owner of intellectual property (according to the so called DEMPE rules, i.e. the concept of development, enhancement, maintenance, protection and exploitation of intangibles). Further, a centralized approach should be introduced for the operationalization of the regime. The tax administration of the jurisdiction where the head office of the corporation is located should play a key role. This tax authority should act as the single point of contact and collect the information that is necessary for the administration of the regime, reallocate and distribute the portion of tax revenue that is assigned to each eligible market jurisdiction. With this setup, administration would be consolidated at the head office level of in-scope corporations. The local tax administration would be in charge of administering the regime and the exchange of information and tax revenue would take place through official channels. Corporations would need to adhere to the requirements of the new regime based on their obligations towards their local tax authority, which would ensure a level playing field.
		b. building on existing mechanisms of double tax relief, such as tax base corrections, tax exemptions or tax credits?	Tax exemption is the preferred option.
		c. ensuring that existing mechanisms for eliminating double taxation continue to operate effectively and as intended?	As mentioned above, harmonizing standards is key. As a general point, potential spill-over effects are a great concern, in particular with regard to legal uncertainty. A new nexus rule must very clearly limit the ability of jurisdictions to use this rule for anything other than Amount A tax purposes (including, for example, filing requirements, other taxes, income or non-income, as well as non-tax issues).
6. Amount B	Given the large number of tax disputes related to distribution functions, Amount B of the “Unified Approach” seeks to		The characteristics of Amount B primarily apply to consumer goods companies. They cannot simply be transferred to the banking industry.

	explore the possibility of using fixed remunerations, reflecting an assumed baseline activity. What challenges and opportunities does this approach offer in terms of simplification and prevention of dispute resolution? In particular, please consider any design aspects and existing country practices that could inform the design of Amount B, including: a. the need for a clear definition of the activities that qualify for the fixed return; and b. a determination of the quantum of the return (e.g., single fixed percentage; a fixed percentage that varied by industry and/or region; or some other agreed method).		In banking, there is no specified distribution function that is clearly distinguishable from production. Moreover, "Limited Risk Distributor" with limited risks and routine functions vis-à-vis a principle company with material risks and entrepreneurial functions is a concept that is not used in banking. Local entities of banking groups assume separate material risks, perform key functions and use/contribute valuable assets, i.e. they are co-entrepreneurial. Instead of remunerating them via cost-plus/TNMM, simple revenue sharing models are often applied. **Amount B effectively does not exist with regard to banking services. This is a reason why IBFed argues for a carve-out of the banking industry.**
7. Amount C/Dispute Resolution and Prevention	In the context of Amount C of the "Unified Approach", what opportunities do existing and possible new approaches to dispute prevention offer to reduce disputes and resolve double taxation? In particular, what are your experiences with existing prevention and resolution mechanisms such as:	a. (unilateral or multilateral) APAs?	
		b. ICAP?	
		c. mandatory binding MAP arbitration?	
Other Comments?			Please see cover letter for SBA's general comments.