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OECD Pillar One – Amount B

On 19 February 2024, the OECD/G20 Inclusive Framework ('OECD Inclusive Framework') published a report on Amount B of Pillar One, outlining a new process for **pricing baseline marketing and distribution activities** which will be treated as providing outcomes consistent with the **arm's length principle** in countries that **opt** to apply Amount B. All businesses, regardless of size, are potentially in the scope of Amount B if they carry out suitable distribution activities.

The OECD Inclusive Framework has been developing a 'two-pillar' approach to international tax reform. Amount B forms part of the Pillar One package on profit allocation. This latest release follows a consultation containing updated design elements of Amount B in July 2023, and a consultation on the main design elements of Amount B in December 2022.

Deloitte comments

The OECD Inclusive Framework has published a further paper on Amount B, designed to simplify and streamline the transfer pricing approach to baseline marketing and distribution activities and to apply from 1 January 2025.

The pricing matrix put forward by the OECD Inclusive Framework retains the simplicity and ease of use from earlier draft proposals, including three industry groups and the use of objective quantitative criteria for selecting the right category in the matrix. It is to be applied on an 'ex post' basis, i.e. testing the transfer pricing outcome at the end of the year. Groups are likely to want to take into account the matrix when setting their prices for in-scope distributors. There are guardrails to ensure that a return on sales does not over-reward businesses that have limited local activity. Further adjustments will be made for countries that have low credit ratings for their sovereign debt, as proposed in earlier drafts, although the economic rationale for doing so remains unclear.

To determine in-scope distributors, groups will apply basic transfer pricing principles (can the distributor be priced using a one-sided transfer pricing method, for example) combined with quantitative factors. Some countries are of the view that additionally they need to apply qualitative factors, so these will be developed in the near future but will be optional for Amount B countries to apply.

Further work is also being done to determine countries that are adopting the Amount B rules either compulsorily for all in-scope distributors within their borders or as an elective mechanism that businesses can choose to adopt, as well as qualifying jurisdictions for various aspects of the rules. It's clear that not all countries in the Inclusive Framework are aligned with the desire for simplicity and a global approach. India, for example, has made a number of reservations against the Amount B approach, but it remains to be seen which countries agree to apply Amount B and which do not. Such optionality at the country level will be concerning for many businesses, as depending on take-up Amount B may fail to deliver the promised transfer pricing simplicity. Businesses will have to check the implementation by countries and adapt their approaches to distribution pricing depending on the viewpoints of the countries involved.

OECD Inclusive Framework countries have committed to respect the outcome of Amount B where it has been adopted by low-capacity countries, including in resolving disputes. Outside of this, the optionality for countries around implementation means that in some, perhaps many, situations there will not be bilateral certainty on applying the Amount B methodology, and normal arm's length pricing assessments and benchmarking will still be required.

The OECD Inclusive Framework has developed a framework for Amount B, which aims to simplify and streamline the application of the arm's length principle to in scope **baseline**

marketing and distribution activities. The framework sets out the scoping criteria, pricing methodology, documentation and tax certainty considerations relating to Amount B.

Scope

Amount B will apply to the following 'qualifying transactions':

- **Buy-sell marketing and distribution transactions** where the distributor purchases goods from another group entity for **wholesale distribution to third parties**; and
- **Sales agency** and **commissionaire transactions** where the entity contributes to the wholesale distribution of goods by another group entity to third parties.

Wholesale distribution includes distribution to any customers except 'end consumers' (i.e., retail distribution). A wholesale and retail distributor is deemed to solely carry out wholesale distribution if its three-year weighted average net retail revenues do not exceed 20% of its three-year weighted average net total revenues.

An accurate delineation of the qualifying transaction will need to be undertaken in accordance with Chapter I of the OECD Transfer Pricing Guidelines. Businesses will then need to determine whether 'baseline' activities are undertaken using the **Amount B scoping criteria**:

- Qualitative criteria: the qualifying transaction must exhibit **economically relevant characteristics** that mean it can be **reliably priced** using a **one-sided transfer pricing method**, with the distributor, sales agent, or commissionaire being the tested party i.e., the simpler party to be tested under the transfer pricing rules.
- Quantitative criteria: a **numerical filter** will apply to specify that the **ratio of annual operating expenses to annual net revenues** of the tested party must be within a range between 3% and an upper bound of between 20% and 30%, based on a three-year weighted average.

Specific transactions are carved out of Amount B (even if they meet the above criteria) where they relate to:

- Transactions involving the distribution and marketing of **non-tangible goods or services** (including digital goods and services) or the trading, marketing or distribution of **commodities**; and
- Transactions where the entity carries out **non-distribution activities** (e.g. manufacturing or research and development) in addition to the distribution activities, **unless** the distribution activities can be **adequately evaluated** and **priced separately** (following a segmentation exercise) from the non-distribution activities.

Application of the most appropriate method to in-scope transactions

The Transactional Net Margin Method is considered the most appropriate method for pricing in-scope transactions. Where 'internal' comparable uncontrolled transactions are available to reliably price in-scope transactions, a limited exception permits the use of the internal comparable uncontrolled price (CUP) method.

Pricing methodology

The OECD Inclusive Framework has used agreed benchmarking search criteria and performed a manual review to produce a **global dataset** of independent parties that undertake baseline marketing and distribution activities. The global dataset has been used to develop a **global pricing matrix** to approximate arm's length returns for in scope transactions, using return on sales as the net profit indicator.

Businesses will determine the return for in-scope transactions by selecting the **relevant segment of the pricing matrix** based on:

- **Industry group**, selected from three groups, which were determined based on observed relationships between specific industries and the levels of returns earned by baseline distributors operating in that sector. A weighted average return is calculated where the products distributed fall into more than one industry group **and** more than 20% of sales are from products which are not in one industry group; and
- '**Factor intensity classification**', selected from five categories based on the business' **net operating asset intensity** (ratio of net operating assets to net revenue – 'OAS') and **operating expense intensity** (ratio of operating expenses to net revenue – 'OES'), calculated based on a weighted average of the business' three preceding fiscal years.

OECD pricing matrix (return on sales %) derived from the global dataset

Industry Grouping	Industry Grouping 1	Industry Grouping 2	Industry Grouping 3
Factor Intensity			
[A] High OAS / any OES >45% / any level	**3.50%**	**5.00%**	**5.50%**
[B] Med/high OAS / any OES 30% – 44.99% / any level	**3.00%**	**3.75%**	**4.50%**
[C] Med Low OAS/any OES 15% – 29.99% / any level	**2.50%**	**3.00%**	**4.50%**
[D] Low OAS / non-low OES <15% / 10% or higher	**1.75%**	**2.00%**	**3.00%**
[E] Low OAS/low OES <15% OAS / <10% OES	**1.50%**	**1.75%**	**2.25%**

Source: Pillar One – Amount B (February 2024) (oecd.org)

Businesses can use the relevant return on sales % derived from the pricing matrix, plus or minus 0.5%.

Appendix B includes eight illustrative examples, which demonstrate how to calculate the return on sales of a business within the scope of Amount B.

An **operating expense cross-check** acts as a corroborative guardrail to test whether the return on sales provided using the global pricing matrix is appropriate, or whether additional adjustments are required. Where the return on sales determined under the pricing matrix, converted into a ratio of earnings before interest and taxes to operating expenses, is **outside** the applicable **operating expense cap-and-collar range**, the return on sales will be adjusted to the **nearest edge** of the range.

The level of the cap and collar is determined by reference to the business' factor intensity classification (see above), adjusted in the case of a 'qualifying jurisdiction'.

An additional adjustment is made in the case of in-scope distributors operating in countries where there is no or insufficient data in the global dataset and the country is a '**qualifying jurisdiction**'. This is referred to as the **data availability mechanism** and requires an uplift to the return to be calculated by multiplying the entity's operating asset intensity percentage for the relevant fiscal year (capped at 85%) by a specified percentage based on the **sovereign credit rating category** of the country applicable on the first day of the relevant fiscal year. For example, countries with a rating of BBB or higher will have no adjustment but countries with a rating of CCC– or lower will apply an upward adjustment equal to 8.6% multiplied by the entity's operating asset intensity percentage.

The analysis underpinning the ranges in the pricing matrix and the operating expense cap-and-collar rates will be updated every **five years** (unless there is a significant change in market

conditions in the interim); the financial data and other datapoints in relation to the pricing matrix and data availability mechanism will be reviewed **annually** and updated **where necessary**.

Documentation requirements

Businesses with transactions within the scope of Amount B will be required to provide information to tax authorities as part of the transfer pricing local file, including:

- **Explanation of the delineation of the in-scope transaction**, including the functional analysis, the parties to the transaction and the context of the transaction (e.g. other commercial or financial relations that may influence accurate delineation of the transaction);
- **The written contract** (if one exists) or agreements governing the transaction;
- **Calculations** of the revenue, costs and assets allocated to the in scope transaction; and
- Information and allocation schedules tying **financial data used** in respect of the scoping criteria and application of the transfer pricing method **to the financial statements**.

Tax authorities can **request further information** relevant to assessing the application of Amount B.

In the first year of application, business should include in their documentation a **consent to apply** Amount B for a **minimum of three years**, unless transactions are no longer in scope during that period or there is a significant change to the business.

Individual country tax authorities may require businesses to provide a **written contract** signed **prior** to the in-scope transactions (but there is no general requirement for a written contract).

Implementation framework

The Amount B rules are optional for countries and have been incorporated into the OECD Transfer Pricing Guidelines as an Annex to Chapter IV (special considerations for baseline distribution activities).

Countries can choose to apply Amount B to in-scope transactions for fiscal years **beginning on or after 1 January 2025**.

Two options are available to countries:

- **Permit** businesses resident within the country to **elect** to apply the simplified and streamlined approach; or
- **Require** businesses to apply the simplified and streamlined approach **where the scoping criteria are met**.

Generally, the outcome of the application of the Amount B approach by a country applying the rules is **non-binding** on the counterparty country unless that country has also adopted the Amount B rules. Subject to their domestic legislation and administrative practices, countries in the OECD Inclusive Framework have **committed to respect** the outcome where it is applied by a '**low capacity jurisdiction**' and to take all reasonable steps to relieve double potential taxation where there is a bilateral tax treaty in place (and it is noted that some countries may choose to extend this commitment to cases where there is no tax treaty).

A business should not rely on the simplified and streamlined approach to justify the position in a country that does not implement Amount B. A **list of countries applying Amount B** will be added to the OECD website.

Tax certainty and elimination of double taxation

Where disputes arise between businesses and tax authorities in relation to the application of Amount B, **existing tax dispute prevention and resolution mechanisms will apply**, including advance pricing arrangements and mutual agreement procedures.

Mutual agreement procedures should not be based on the baseline marketing and distribution approach under Amount B if one or more of the relevant countries has not chosen to apply or accept this approach. Countries may provide a **corresponding adjustment** that reflects the outcome of applying Amount B on a case-by-case basis if it is considered to produce an acceptable outcome in that specific case.

Any agreement (including mutual agreement procedure cases and bilateral or multilateral advance pricing agreement cases), obtained prior to the implementation of Amount B will continue to be valid.

Next steps

The OECD Inclusive Framework is working on an additional 'optional' qualitative scoping criterion that jurisdictions may choose to apply to identify distributors performing '**non-baseline activities**'. Work on this will be concluded by 31 March 2024, with any additions to be incorporated into the OECD Transfer Pricing Guidelines.

'**Qualifying jurisdictions**' for the purposes of the operating expense cross-check and the data availability mechanism are to be fixed **prospectively** based on qualifying criteria to be incorporated into the guidance in a subsequent update. The lists of qualifying jurisdictions will be published and updated every **five years** on the OECD website.

The OECD Inclusive Framework will undertake further work on the implementation of the commitment of countries to respect the outcome of Amount B where it is applied by a low capacity jurisdiction (including through the development of competent authority agreements) in **2024**. The list of **low capacity jurisdictions** will be agreed by the OECD Inclusive Framework by **31 March 2024** and published on the OECD website.

Information will be gathered on the **practical application of Amount B**. Consideration could be given to producing **further implementation guidance**, if needed.

Further work is to be undertaken on the interdependence of Amount B and Amount A under Pillar One prior to the signing and entry into force of the Amount A multilateral convention.

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