Additional Guidance on Amount B of Pillar One released by OECD/G20 Inclusive Framework

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Issue 4

In brief

On 17 June 2024, OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (Inclusive Framework or IF) released additional guidance on Amount B of Pillar One (Additional Guidance), which provides supplementary elements relating to the report on Amount B of Pillar One published on 19 February 2024. The Additional Guidance includes:

	Subject	Key content	Application to China
Additional Guidance Part I	The definitions of qualifying jurisdictions within the meaning of section 5.2 and 5.3 of the Amount B guidance.	These definitions will facilitate adjustments to the return calculated under the simplified and streamlined approach for tested parties located in those qualifying jurisdictions. The respective definitions are now incorporated into the Amount B guidance in the annex to Chapter IV of the OECD Transfer Pricing Guidelines.	China is a qualifying jurisdiction within the meaning of section 5.2 while not a qualifying jurisdiction within the meaning of section 5.3
Additional Guidance Part II	The definition of covered jurisdictions within scope of the political commitment on Amount B	That political commitment recognises that subject to their domestic legislation and administrative practices, members of the Inclusive Framework commit to respect the outcome determined under the simplified and streamlined approach to in-scope transactions where such an approach is applied by a covered jurisdiction and to take all reasonable steps to relieve potential double taxation that may arise from the application of the simplified and streamlined approach by a covered jurisdiction where there is a bilateral tax treaty in effect between the relevant jurisdictions.	China is a member of Inclusive Framework while not a covered jurisdiction

In detail

Additional Guidance Part I: The definitions of qualifying jurisdictions within the meaning of section 5.2 and 5.3 of the Amount B guidance.

- **Section 5.2 of the Amount B guidance (Operating expense cross-check):** Amount B guidance defines an operating expense cap-and-collar range for the operating expense cross-check. Alternative cap rates where the tested party is located in a qualifying jurisdiction is higher than the default cap rates. Qualifying jurisdictions refer to jurisdictions that are classified by the World Bank Group as low income, lower-middle income, and upper-middle income based on the latest available 'World Bank Group country classifications by income level'.
- **Section 5.3 of the Amount B guidance (Data availability mechanism for qualifying jurisdictions):** The data availability mechanism provides for upward adjustments to the returns otherwise derived from the pricing matrix where there is no or insufficient data in the global dataset for a particular tested party jurisdiction which could be reasonably considered a 'higher risk' jurisdiction. Qualifying jurisdictions refer to jurisdictions with a publicly available long term sovereign credit rating2 of BBB+ or lower, and with less than 5 comparables in the global dataset. European Union member countries is excluded. A jurisdiction without a long-term sovereign credit rating and with less than 5 comparables in the global dataset will nevertheless be regarded as a qualifying jurisdiction if it is classified by the World Bank Group as low income, lower-middle income or upper-middle income.

Pleases refer to the Additional Guidance on the list of the above qualifying jurisdictions. The list of qualifying jurisdictions will be published and updated every 5 years on the OECD website.

It is worth noting that China is a qualifying jurisdiction within the meaning of section 5.2 but not a qualifying jurisdiction within the meaning of section 5.3.

The list of qualifying jurisdictions does not imply that these jurisdictions are obligated to adopt or will adopt the simplified and streamlined approach.

Additional Guidance Part II: The definition of covered jurisdictions within scope of the political commitment on Amount B

That political commitment recognises that subject to their domestic legislation and administrative practices, members of the Inclusive Framework commit to respect the outcome determined under the simplified and streamlined approach to in-scope transactions where such an approach is applied by a covered jurisdiction and to take all reasonable steps to relieve potential double taxation that may arise from the application of the simplified and streamlined approach by a covered jurisdiction where there is a bilateral tax treaty in effect between the relevant jurisdictions.

List of Covered Jurisdictions for the Inclusive Framework political commitment on Amount B is listed below. The list of covered jurisdictions would be published on the OECD website. The list of covered jurisdictions will be reviewed every 5 years.

- Albania
- Angola
- Argentina
- Armenia
- Azerbaijan
- Belarus
- Belize
- Benin
- Bosnia and Herzegovina
- Botswana
- Brazil
- Burkina Faso
- Cabo Verde
- Cameroon
- Egypt
- Eswatini
- Fiji
- Gabon
- Georgia
- Grenada
- Haiti
- Honduras
- Jamaica
- Jordan
- Kazakhstan
- Kenya
- Malaysia
- Maldives
- Nigeria
- North Macedonia
- Pakistan
- Papua New Guinea
- Paraguay
- Peru
- Philippines
- Saint Lucia
- Saint Vincent and the Grenadines
- Samoa
- Senegal
- Serbia
- Sierra Leone
- South Africa

- Congo
- Costa Rica
- Côte d'Ivoire
- Democratic Republic of the Congo
- Djibouti
- Dominica
- Dominican Republic
- Liberia
- Mauritania
- Mauritius
- Mexico
- Moldova
- Mongolia
- Montenegro
- Morocco
- Namibia
- Sri Lanka
- Thailand
- Togo
- Tunisia
- Ukraine
- Uzbekistan
- Viet Nam
- Zambia

The list of covered jurisdictions does not imply that these jurisdictions are obligated to adopt or will adopt the simplified and streamlined approach. In addition, China is a member of Inclusive Framework, but not a covered jurisdiction.

For example, if a Chinese enterprise enters into buy-sell transactions with an affiliated distributor located in a covered jurisdiction, the Chinese enterprise needs to consider the following:

- Is the affiliated distributor an eligible baseline distributor?
- Is the related party buy-sell transaction a qualifying in-scope transaction?
- Does the covered jurisdiction adopt the simplified and streamlined approach?
- As a member of Inclusive Framework, will China take reasonable steps to relieve potential double taxation that may arise from the application of Amount B regarding the related party transactions between the Chinese enterprise and the affiliated distributor based on the Amount B guidance?

The takeaway

The implications of the Additional Guidance for China are mainly in the following areas:

- Although China is a qualifying jurisdiction within the meaning of section 5.2, since Section 5.2 simply refers to the operating expenses cross-check for adjustments to the return calculated based on Amount B, China will not be affected by Section 5.2 in substance if China does not adopt Amount B;
- It remains unclear whether China, as a member of the Inclusive Framework, will take all reasonable steps to relieve potential double taxation that may arise from the application of Amount B.
- We recommend that in addition to focusing on the impact of Pillar Two, Chinese outbound enterprises will need to closely monitor the local legislative process on Amount B of Pilar One for the covered jurisdictions where their distribution affiliates are located. Analysis of the applicability of Amount B should be carried out, including reviewing the marketing and distribution arrangements that have already been implemented within the group, identifying the businesses or operations that may potentially be affected by Amount B, and assessing the risk exposure by comparing the current profit level of the in-scope transactions or entities with the profit margins set out in the pricing matrix of Amount B;
- Based on our observation, in China's transfer pricing practice, some tax authorities have considered the applicability of Amount B in transfer pricing investigations and advanced pricing arrangements. However, no conclusion has yet been reached as to whether the application of Amount B is consistent with the arm's length principle, and there are differing views amongst tax authorities nationally.

Endnote

1. Members of the OECD/G20 Inclusive Framework on BEPS includes 147 countries and regions as of May 2024. China is a member of Inclusive Framework.

2. According to the Additional Guidance, the criteria relevant for determining the list of covered jurisdictions are as follows:

- Low- and middle-income IF jurisdictions using the World Bank Group country classifications by income level, excluding EU, OECD, and G20 member countries.
- Extend to low- and middle-income IF jurisdictions that are OECD and G20 member countries that otherwise satisfy the first criterion and that expressed to the Inclusive Framework a willingness to apply Amount B by March 2024.

- Any non-IF member that meets the first criterion and expresses to the Inclusive Framework a willingness to apply Amount B will be added to the list of covered jurisdictions.3

China, as a middle-income IF jurisdiction that is a G20 member country, is not a covered jurisdiction, suggesting that China has not expressed to the Inclusive Framework a willingness to apply Amount B by March 2024.

Let's talk

For a deeper discussion of how this impacts your business, please contact **PwC's China Transfer Pricing Service Team**:

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