Business at OECD

20 May 2022

To: Tax Treaties, Transfer Pricing and Financial Transactions Division
Organisation for Economic Cooperation and Development
Centre for Tax Policy and Administration
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Submitted by email: tfde@oecd.org

Re: *Business at OECD* (BIAC) comments to OECD's Public Consultation Document "Pillar One – Amount A: Regulated Financial Services Exclusion"

Dear Secretariat Team,

Thank you for the opportunity to comment on the public consultation document "Pillar One – Amount A: Regulated Financial Services Exclusion" (the "Document"). We provide our more detailed comments in the attached but wish to call particular attention to the following points in our response.

- We support the exclusion for Regulated Financial Services ("RFS") activities and its policy goal, as expressed in the Background section that the exclusion is based on unique regulatory drivers that generally helps to align the location of profits with the market. We therefore acknowledge the fact that the Model Rules would be designed on that principle.

- Achieving this objective requires a careful framing of the rules to ensure that profits from RFS activities are not inadvertently allocated to market jurisdictions under Amount A. We agree with the policy statement in the Document that outcomes in respect of the in-scope activities undertaken by the Group should equate to the outcomes of a standalone business separate from the RFS activities part of the Group – this would ensure appropriate outcomes under Amount A and a level playing field with Groups that are not engaged in RFS activities but are engaged in similar in-scope activities.

- As a starting point, the Document indicates that some members believe that reinsurance and asset management ought not to be excluded from Amount A. We disagree with this point for reasons below.

    - As discussed in our detailed comments, below, Asset Managers are prudentially regulated, put up capital against risk-based measures and are subject to extensive regulatory supervision much like other Regulated Financial Institutions ("RFIs"). In addition, the activities carried out by financial services firms are very integrated, and not including Asset Managers within the RFS Exclusion will create disparity in treatment, under Pillar One, between like services performed by various regulated Entities within a Group.

    - Likewise, Reinsurance satisfies the key elements of the definition of Regulated Financial Services as set out in this Document: that is licensing, regulatory capital

and supervision and activities requirements. In these respects Reinsurance is identical to Insurance and it is difficult to see why it should be treated differently.

- By virtue of some financial services not being covered under the RFS Exclusion, the Document seeks to put forward several approaches to determine whether a Group is subject to Amount A where both the revenue and profitability thresholds would otherwise be met for in-scope activities. We believe this creates much complexity, cost and administrative burden on both taxpayers and tax administrations. We have put forward a very simple rule by which all third party revenue of an RFI should be considered out-of-scope. That is how regulators view and supervise RFIs and, thus, is a standard to apply here. We also urge further simplification of Step 3, which the Secretariat admits is the more complex part of the Document. Preparing bespoke financial statements would cause tremendous burden for MNEs when other reliable data already exist. We have proposed some simplification mechanisms for your consideration in our detailed comments below.

- It is equally important that early certainty is provided for all aspects of the RFS Exclusion, including determination of out-of-scope and in-scope financials, for example. Further, as the financial services industry and its associated regulations are constantly evolving, we believe a 5-year review should apply to all the activities tests of all RFIs (i.e., activity lists and thresholds), so that such tests are kept up to date with industry developments. Finally, taxpayers should be able to re-obtain tax certainty if such periodic reviews cause significant changes to their Amount A calculations.

We thank you for the opportunity to comment. We would be pleased to respond to any questions arising from both our general and specific comments provided, and to providing further support and assistance in implementation efforts to follow.

Sincerely,

Alan McLean
Chair, *Business at OECD* (BIAC) Tax Committee

William H. Morris
Chair Emeritus

Cc: Hanni Rosenbaum, Executive Director, *Business at OECD* (BIAC)

Our detailed comments are provided below:

Para	Topic	Issue	Recommendation
Backgro und	Definition of RFS	Diverging views within the TFDE regarding the exclusion of asset managers from the scope of Amount A.	Asset Managers should be part of the RFS Exclusion. Asset Managers are prudentially regulated which requires a significant amount of capital to be set aside in order to conduct business in a manner determined and akin to Depositary, Investment and Insurance Institutions. Required capital is based on financial and capital market risk-based measures and are likewise subject to ongoing and extensive regulatory supervision. • For instance, retail asset management is highly-regulated operating under significant and specific legal, regulatory, and tax frameworks. Retail asset management is largely distributed by intermediaries in the form of banks, insurance companies and brokers, all of which are subject to appropriate regulatory regimes, so there is no real distinction between retail asset management and other components of the regulated financial services sector. Distribution activities are already subject to taxation in the market jurisdictions as those profits are mainly driven by the business of the intermediary. The nature and extent of Asset Management prudential regulation dictates that profits arise locally. In fact, some jurisdictions, by express regulation, only permit certain products (e.g., retail funds) to be sold, locally. Where activities to provide Asset Management products and services arise in a cross-border context either by the Asset Manager or by another RFI(s), and if they touch an otherwise prudentially regulated Entity, the revenues and profits of such activities should be part of the RFS Exclusion.

Para	Topic	Issue	Recommendation
			Furthermore, the provision of financial services to clients is highly integrated and seamless, even though many Entities within a Group typically carry out different activities oftentimes through prudentially regulated Entities. Depositary, Investment and Insurance Institutions own or are owned by Asset Managers. It is important that a level playing field be assured within the RFS Exclusion lest inequitable Amount A outcomes will be created.

Background Para 19 FN 6	Definition of RFS	Diverging views within the TFDE regarding the exclusion of reinsurance from the scope of Amount A.	Reinsurance services fulfil the key requirements of the definition of Insurance Institution in para 23, that is a licensing requirement, a solvency requirement incorporating a risk-based capital measure and the derivation of gross income from insurance contracts (reinsurance contracts are simply insurance contracts of primary insurance contracts):
			- Reinsurance is regulated under similar rules as those applicable to the insurance industry and reports to similar supervisory bodies.
			    o There are regulatory requirements upon entry to a given market (prior authorisation or licensing depending on the local regulation).
			    o Supervision rules include verification of solvency, assets, and eligible own funds.
			- Reinsurance is simply insurance for insurers; in the same way consumers buy insurance to lay off their exposure to risk, insurers buy reinsurance to manage their risk. Reinsurance pursues the same business model as insurance by contracting with a primary insurer to reimburse any future claims that primary insurer may have against the payment of a premium. Reinsurance is a business-driven commercial transaction that is both functionally and economically integrated with the writing of primary insurance.

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			Furthermore, reinsurance is based on the diversification and pooling of risks on large scales on a global basis to mitigate losses due to major claims or natural catastrophes that may arise in specific areas. There is, therefore, often little connection between the location of revenues (premiums) received in a particular year and the location of the profits arising in that year. Diversification means that, for example, the risk of rainstorm in Europe may be offset against hurricane risk in the Gulf of Mexico. Premiums are received from both locations, but one may produce profit and the other losses, resulting in a net profit or loss that cannot be allocated jurisdictionally on the basis of premiums received. In addition, reinsurance profits may also take many years to realise, depending on the nature of the underlying risk. For example, risk reserves relating to industrial disease may not be released to profit for several decades, after which time the location of the original revenues may not be known. Including reinsurance in the scope of Amount A could therefore lead to adverse results by allocating taxing rights to jurisdictions where the reinsurer incurs losses, based on profits generated elsewhere through the built-in diversification process of pooling risks. With respect to the key RFS requirements, reinsurance is no different from insurance and it is unclear therefore why the discussion draft identifies reinsurance separately from insurance. We welcome the exclusion of reinsurance as a RFS from the scope of Amount A and recommend that it be more explicitly confirmed. For instance, wherever Insurance Institutions are mentioned, the Model Rules should mention both “insurance” and “reinsurance”.

Para	Topic	Issue	Recommendation
4	Use of an Entity approach	Many in the industry thought a consolidated approach whereby if a certain percentage [e.g., 70%] of all the activities of the consolidated group were excluded activities, then the entire group would be excluded. The IF has instead chosen to use an Entity approach.	We believe the Entity approach is a viable approach. However, it does create certain issues, as discussed below, which necessitates certain changes to the draft.
11-18	Mechanics of Step 2	Given large RFIs may have upwards of hundreds of Entities, the top-down approach should work well to reduce the work that would otherwise be required if each Entity needed to be tested. For instance, one large bank has concluded they will only have to test five Entities. While we very much support this approach, we would like to propose a further, albeit elective, simplification method.	We note that the computation of separating third party revenues from related party revenues is done for the Country by Country (CBC) report. While CBC reports require this information on a jurisdictional basis, it is often the case that the jurisdictional number is built up from separate Entity numbers. Consequently, we believe that it would be appropriate to allow a taxpayer to elect to utilize these entity-level CBC numbers and a presumption that they are accurate.
13	Determination of in-scope revenues from financial services	In practice, many RFIs provide integrated financial services to clients, oftentimes through one point of contact even though such services are likely performed across different Entities within the consolidated group. A simple example which is prevalent and rather common across the financial services industry: • An Insurance Institution offers an Investment Fund to one of its clients. The Investment Fund is distributed by an affiliated Investment Institution, the monies are managed by an affiliated Asset Manager, the Investment Fund's assets are held by an affiliated custodial (presumably, an Investment Institution), and various other Group Entities perform other related services such as investor reporting, compliance, research, trading and operations. In these regards, a single client's fee is likely to be shared amongst all involved Entities for	For Step 2 to appropriately address this integrated service approach endemic to financial services, we recommend that all third party revenue derived by an RFI be considered as RFI revenues. This is consistent with the policy intent of the RFS Exclusion. It is also how a prudential regulator supervises such RFI and how revenues are reflected in the Entity's financial statements filed with such regulator.

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		various reasons be they for regulatory, management or compensation purposes. In addition, where an Entity is an RFI, prudential regulation covers all of such RFI's activities. That is, regulatory capital on a risk-based measure is required on both direct and indirect third-party clients of an RFI. Here, unless each involved Entity neatly fits into each RFI definition, out-of-scope revenue, despite it being attributable to that single client could be unduly created.	
13-14	Determination of in-scope revenues from financial services	How to best align the RFI Exclusion, Step 2 subtraction, Step 3 profitability computation and, ultimately, determination of Amount A (where the in-scope revenue and profitability thresholds are met).	This alignment is important to the policy outcome of Pillar I. Thus, we recommend that the Step 2 and 3 tests should focus on the Entity's activities and revenues and profits therefrom and thereby follow that same principle as para 38 (i.e., by treating the in-scope activities as a separate and independent business from the RFIs).
18	Definition of RFS; Schedule G	Footnote 5 - we appreciate the principles put forward around what constitutes acceptable regulation for purposes of the RFS Exclusion. We also appreciate the OECD's acknowledgement that not all regulation is the same across national borders or within the financial services industry, and the perspective that neither the OECD nor tax administrations are well-equipped or appropriate arbiters of the condition b. standard being applied throughout the RFS Exclusion. However, we are concerned that, in practice, tax administrations may take differing views on the high level and principles-based regulatory standard in this document.	Thus, it is critical to review condition b. as part of the early certainty process ("ECP"). ECP, dispute prevention and resolution for the entire RFS Exclusion should also be dealt with in a fashion similar to how other potential questions and controversy will be addressed throughout Pillar I.
20(a); 21(a); 22(a);	Licensing Requirement	These paragraphs require that the Entities be licensed to carry out certain activities as laid out in (c). The language set out could be read to require that the license must	It should be made clear that a license does not have to enumerate all of the items listed in (c) but rather under the rules of a given jurisdiction, be understood to allow the Entity

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23(a); 24(a); and 25(a)		specifically enumerate all of the activities listed in (c). That will generally not be the case. Rather the license may simply say that the Entity is licensed to conduct a banking, broker dealer, insurance or investment management business.	to conduct the activities generally conducted by, for example, a bank.
20(c, d); 21(c, d); 22(c); 23(c); 24(c); and 25(c)		Any lists or thresholds included in the activities tests will likely become inadequate after a period of time.	We recommend that these lists and thresholds be updated at least every five years.
20(c)	Requirements for a Depositary Institution - engaging in certain activities	There are activities other than those listed in footnote (9) in which Depositary Institutions engage. If the rule is meant to be that a Depositary Institution engages in one or more of these activities then the list does not need to be expanded for other ordinary course activities in that it is very unlikely that a Depositary Institution will not engage in one of the activities listed. But this conclusion may be critically impacted as to certain issues pertaining to Mixed Financial Institutions (see below).	It should be made clear that a Depositary Institution need engage in just one of the activities listed in footnote 9, and is not precluded from being a Depositary Institution if it also engages in licensed activities that are not on the footnote 9 list. If, however, certain issues with respect to Mixed Financial Institutions are clarified in certain ways (see below), then it would become critical that the list in footnote 9 be greatly expanded.
21	Mortgage Institution	We ask whether there is a policy rationale for condition c. being limited to credits granted solely to individuals for the purchase (or refinancing) of real estate. For instance, why aren't commercial mortgages, credit card loans and automobile loans included, subject to not being granted for the purchase (or refinancing) of a Group Entity's own goods (i.e., a captive financing Entity, per footnote 14)?	We recommend that Mortgage Institution definition be modified to 'Financing or Credit Institution,' subject to conditions a-c, as with other RFIs (but exclude captive financing Entities). This would level the playing field amongst financial services firms that provide credit.[1]

[1] We also note that leasing companies (other than those that are related to the seller of the leased product) are not specifically excluded. We are aware of some leasing companies that are part of a banking group which are licensed and subject to regulatory capital requirements. It is our position that these types of entities should be excluded under the existing rules (or should be under a separate exclusion).

Para	Topic	Issue	Recommendation
22(c)	[75%] gross income requirement for Investment Institutions	Para 22(c) requires that gross income attributable to a specific list of activities equals or exceeds [75%] of gross income.	The list as set forth is inadequate if paired with the 75% requirement. For example, hedging of our own positions is not included; lending other than in connection with acquisition transactions is also not included; repurchase agreements and margin loans are not covered; further, revenues from securities loans are not included. We suggest the OECD work with the industry to develop a more complete list.
23(c)	Definition of gross income	Insurance groups may report their premiums in their financial statements on a gross (premiums received from policyholders) or net (after reinsurance) basis.	For the avoidance of doubt, it would be helpful to explicitly state that gross income in the context of para 23(c) includes gross premiums.
23(c)	Investment income	Para 23(c) includes investment income from assets associated with insurance and annuity contracts in gross income, but is unclear as to what 'associated' means. Insurance entities are required to hold regulatory capital to support risks arising from insurance/annuity contracts, which may be in excess of the assets they hold from premiums. Where an asset is held to support risk reserves or regulatory capital, that is a fundamental business asset and any associated income should be included in gross income for the purposes of the [75%] test.	We suggest the Commentary clarifies the phrase 'associated with such contracts' such that income from all assets held to support insurance reserves and capital is included in gross income for the [75%] test.
23(c)	Investment income	Insurance groups often hold and manage investment assets that support insurance liabilities through subsidiaries.	If an investment subsidiary has a majority owner which is an Insurance Institution, the investment subsidiary should also be considered a Regulated Financial Institution and accordingly the investment income earned through those investment subsidiaries should be included in the RFS exclusion. (Majority ownership rather than wholly owned subsidiaries is the required condition, as insurance companies often invest alongside third party investors).
23/FN18	Treatment of Insurance Institutions that provide	Footnote 18 confirms that, where an entity meets the definition of Insurance Institution and provides the activities in para 23(c) to other RFIs in the same Group, that entity is included in the exclusion.	We agree with the intention of this wording, but would note that it is not totally clear. It would be helpful to have a positive confirmation that intra-group-reinsurance within an insurance

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	reinsurance to Insurance Institutions in the same Group.		group is treated the same as reinsurance business with third parties.
24	Asset Manager	The activities listed in condition c. are not sufficient to cover the activities of an Asset Manager.	The list of eligible activities should include risk management and asset management-related operations. Furthermore, we suggest that the Commentary clarify that 'distribution' in this context incorporates the sales and marketing functions of an Asset Manager. See footnote 20 which reflects an intention to be expansive as to assets covered.
25	Mixed Financial Institutions	As currently drafted, this definition applies to entities that are licensed to take deposits but does not allow those entities to include "banking or similar business" activities in the revenue test. This can give rise to unintended results and can greatly reduce the utility of this definition to deposit-taking entities that do not meet the Depositary Institution definition. This is best explained through an example: a Depositary Institution whose preponderance of revenue is generated from loans also engages in interest rate swaps; which are a common activity for banks but not listed in footnote 9. It would appear that since the bank engages in a non-footnote-9 activity, it now has to qualify as a Mixed Financial Institution in that the swap activity is an Investment Institution activity. Further, with respect to that activity there is a requirement that [75%] of the Entities' gross income has to be from the Investment Institution activity. In this situation the predominant activity of the Entity is the loan activity and therefore the	If the [75%] income requirement is to remain, the list of covered activities should be expanded to include "banking or similar business" activities. If not, remove the [75%] requirement at least where such activity is being conducted in an otherwise Depositary Institution.

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		75% requirement cannot be met and the bank is no longer an excluded Entity.	
25	Mixed Financial Institution	Whether a separate definition for Mixed Financial Institution is appropriate.	Yes, providing for this type of RFI is important in addressing the integrated nature of financial services. In this regard, we ask that all RFIs be covered in this definition and the suggested aggregation of activities be engaged.
25	Mixed Financial Institutions	Subparagraph (a) of the Mixed Institution definition refers to a Depositary Institution, but this is not repeated in subparagraph (c).	We would like to ask the Secretariat to clarify the intent of this discrepancy.
26	RFI Service Entity	We are concerned that the meaning of "exclusively" will, in practice, lead to potential disputes.	We suggest that words such as "principally", "primarily", "substantially" be used instead of "exclusively", or establish a numerical threshold such as [90%].
26/FN23	RFI Service Entity	Within the EU, there is a regulatory requirement that employees of an insurance entity can only work for that entity. To avoid duplication and to allow employees to service more than one insurance platform, it is common practice in the insurance sector for the majority of staff, including customer facing staff, to be employed in a service company. Where customer facing staff are employed, the company will be subject to conduct regulation. These service companies have delegated underwriting authority and are remunerated on an arm's length basis, like third-party agents, in the form of a commission (not a cost-plus service fee).	As written, footnote 23 excludes customer facing insurance service companies, even though the staff are performing the same functions as those in Insurance Institutions – i.e., in para 23(c). This is an insurance sector-specific issue, we suggest the OECD work with the industry to consider how insurance service companies with delegated underwriting authority can be included in the definition of RFI Service Entity.[2]
27	Definition of Deposit - principal repayable at par requirement	In some cases, deposits are made in local currency (LC) to be held in a USD account. LC is converted into USD and Interest is paid in USD. When the deposit is withdrawn it is paid in LC based on the then current value of the USD balance.	Such situations should be viewed as principal which is payable at par looking at the currency in which the deposit is recorded and tracked. Further, provided the payout is based on the value of that same currency at withdrawal, it should not matter whether the payment is made in local currency.

[2] We also note that other financial services firms have service entities akin to what is expressed here relative to Insurance Institutions.

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29	Definition of Insurance Contract	The list of covered risks at para 29 is not sufficiently comprehensive - for example, longevity or cyber risks are not listed.	For the avoidance of doubt, it should be stated that the list in para 29 is not exhaustive. We suggest the following modifications to para 29: "Insurance Contract" means a contract of insurance or reinsurance (other than an Annuity Contract) under which the issuer agrees to pay an amount upon the occurrence of a specified contingency involving **risks, including but not limited to,** mortality, morbidity, longevity, accident, liability, or property loss risk. It also includes a contract under which a participant agrees to contribute to a common fund providing for mutual financial benefits payable to the participants or their beneficiaries upon the occurrence of a specified contingency involving **risks, including but not limited to**, mortality, morbidity, longevity, accident, liability, or property loss risk.
31-39	Identifying Excluded and In Scope Profits (Step 3)	There are RFIs that are owned as part of a larger consumer products Conglomerate Group. They may include a Bank, a Life Insurance Company, and a Property and Casualty Insurance Company. These Entities are operated separately but are included in a Finance Group of the Conglomerate which is regulated by the Financial Services Agency of the home country. The Financial Group operations require licenses and capital maintenance based on risk. These Entities do not include group treasury centers or captive insurance companies. The Conglomerate prepares audited consolidated financials including the Finance Group. The Finance Group also prepares separate audited financials for the Finance Group that include some de minimis related activities (e.g., a licensed nursing home) that are not separately subject to review by the Financial Services Agency but are included in the overall capital requirements. The Regulatory Agencies review the	1. Where there are separate audited financials of an RFI group, such financials should be used to separate the excluded RFI group results from the Conglomerate Group's results for purposes of determining in-scope activity, notwithstanding the inclusion of de minimis non-qualifying activities conducted by Entities within the RFI group. This alleviates the significant burden of separating the Conglomerate's audited financials into "bespoke" in-scope and "bespoke" out-of-scope unaudited financials that would require significant system changes and, in the end, would not be materially different than the existing audited financials. 2. In determining whether a financial sub-group of Entities applies as RFIs, a predominance test should apply to the consolidated sub-group's activities so that de minimis activities in separate Entities would not have to be separated from the RFI financials in order to make the separation of in-scope and out-of-scope revenues and

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		Finance Group's audited financials (which includes these de minimis activities) and establishes capital requirements based on those financials. They also review the standalone financials of the bank and the insurance companies. The regulated banking and insurance businesses represent 90% or more of the total revenues and profits of the consolidated Finance Group.	profits practical and administrable. We propose a threshold of [90-95%] for this predominance test. 3. Creating "bespoke" financials for purpose of this exclusion creates a tremendous burden for those large conglomerates that may have a regulated financial group as one of their lines of business. Most will have separate audited financials for the financial line of business in order to submit to the regulatory agencies, and most are subject to prudential regulations and carry out activities set forth in condition c. Thus, those separate financials should be relied upon for the out-of-scope exclusion. This would be simple and clear to implement and transparent for the tax auditors that will review the Conglomerate's remaining in-scope revenues and profits for purposes of calculating Amount A.
N/A	Identifying Excluded and In Scope Profits (Steps 1- 3)	While revenues (and profits) of Excluded Entities are not intended to be counted in Steps 1-3 (see footnote 7), we are concerned that such exclusion can be overly inclusive. That is, where a financial services firm owns a majority interest in a fund, which is not an Investment Fund (as defined, see below question) and which is consolidated in the Consolidated Financial Statements, in determining its Total Revenues under Step 1, satisfaction of condition c. threshold and profitability in Step 3 to, ultimately, compute its Amount A, it appears it would to have to include 100% of the fund's revenues and profits. Of course, this is not economically earned by the affected Entity. In addition, what is the definition of an Excluded Entity and Investment Fund for purposes of this RFS Exclusion, as there are subtle differences in such definition in other	We believe the affected Entity should include only its own ownership percentage in a consolidated fund when computing its third party revenues in Step 1, threshold percentage under condition c. of Step 2, profitability in Step 3, and Amount A in general. This comment is consistent with similar comments we submitted in response to the Scope and Tax Base consultations. For clarity, both Excluded Entity and Investment Fund should be defined here or defined by express reference to other Pillar I (or II) provisions.

Para	Topic	Issue	Recommendation
		Pillar I (and II) provisions, i.e., the 85% test of an Investment Fund in Pillar II?	
N/A	Treatment of transfer prices	There is no articulation of how to determine intercompany revenues and costs between in-scope and out-of-scope Entities.	We believe that the arm's length intra-group price should be respected as part of determining intra-group revenues and costs. To do otherwise risks further complexity and disputes.
N/A	Revenue sourcing	How to apply the revenue sourcing rules for in-scope activities.	Specific industry-relevant revenue sourcing rules beyond those already included in the Revenue Sourcing public consultation are necessary. For instance, Asset Managers distribute their products through RFIs (e.g., be they Depositary, Investment or Insurance Institutions as well as other financial services firms). Often, Asset Managers have no knowledge of who the end investor (consumer) is or where it is located – by virtue of intermediary proprietary information, regulation, data protection laws or the nature of the products, themselves (e.g. publicly-traded funds). Determining to whom Amount A should be allocated will be very challenging, costly and complex. And, we would expect that any Amount A allocations from Asset Managers will often be within the same countries where they already are physically engaged in business, locally taxed and prudentially regulated. Another more specific example is that in the case of retail asset management, the interactions are largely conducted between consumers and financial intermediaries and any contact between the asset manager and the consumer is only indirect. Therefore, the asset manager does not have access to end user data, as they are only held by the intermediary. Therefore, a proper allocation of revenues of the asset management industry to the various consumer jurisdictions involved would be a challenging exercise.

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			Similarly, a reinsurance contract will often cover primary insurance policies written in multiple jurisdictions. In some cases, data protection laws or confidentiality (e.g., Kidnap and Ransom insurance) mean that the reinsurer does not know the location of insured risk. For these policies determining to whom Amount A should be allocated may not be possible or may be very challenging and complex.