

TECHNICAL NOTE

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12

UNPACKING THE AMOUNT B RULE
OF PILLAR ONE AND HIGHLIGHTS
OF ITS POTENTIAL BENEFITS TO
AFRICAN COUNTRIES



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AFRICAN TAX
ADMINISTRATION FORUM

FORUM SUR
L'ADMINISTRATION
FISCALE AFRICAINE

1 INTRODUCTION

This Technical Note is the twelfth in the ATAF Technical Note series on the tax challenges arising from the digitalisation of the economy and has been designed to provide ATAF members with an overview of the Amount B rule of Pillar One which was agreed upon in February 2024.

The Amount B rule was incorporated into the OECD Transfer Pricing Guidelines on 19th February 2024 and provides an optional simplified and streamlined approach that jurisdictions can choose to apply to qualifying transactions of in-scope distributors resident in their jurisdictions. However, there were still some definitions within the rules that were not agreed upon at the time of the publication of this rule.

As the Inclusive Framework has now agreed on those definitions, ATAF is publishing this Technical Note to assist ATAF members in deciding whether to enact the optional simplified and streamlined approach.

The Note provides an overview of the main provisions of the approach and highlights the areas which ATAF considers to be of particular importance for African countries.

In addition, ATAF will shortly publish a revised version of the ATAF Suggested Approach to Drafting Transfer Pricing Legislation that includes provisions countries could include in their transfer pricing legislation and regulations to enact the optional simplified and streamlined approach.

Many ATAF members have reported that transfer pricing issues relating to in-country distribution activities are a major area of dispute and are a significant drain on their limited transfer pricing resources. The optional simplified and streamlined approach, which countries can choose to apply for fiscal years commencing after 1st January 2025, provides an opportunity for African countries to reduce the number of such disputes and create greater tax certainty for both African tax administrations and business.

This Technical Note highlights the design features ATAF considers of most importance if Amount B is to maximise benefits to African countries by increasing tax certainty for both African governments and multinational enterprises (MNEs) operating in Africa.

2 KEY DESIGN FEATURES OF THE OPTIONAL SIMPLIFIED AND STREAMLINED APPROACH

2.1. SCOPE OF THE RULE

The following intra-group transactions are qualifying transactions for the simplified and streamlined approach:

- a. Buy-sell marketing and distribution transactions where the distributor purchases goods from one or more associated enterprises resident in other jurisdictions for wholesale distribution to unrelated parties; and
- b. Sales agency and commissionaire transactions where the sales agent or commissionaire contributes to one or more associated enterprises' wholesale distribution of goods to unrelated parties.

ATAF called for the scope of Amount B to be very broad to maximise the benefits of Amount B for African and other developing countries with limited transfer pricing capacity and for it to therefore include sales agents and commissionaires. We were successful in having these included in the optional simplified and streamlined approach.

A qualifying transaction will be subject to the simplified and streamlined approach when it satisfies all of the scoping criteria summarised below:-

- a. 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.
 - b. The tested party in the qualifying transaction must not incur annual operating expenses lower than 3% or greater than an upper bound of between 20% and 30% of the tested party's annual net revenues.
- A qualifying transaction that meets the above criteria will nonetheless be out of scope if:
- a. The qualifying transaction involves the distribution of non-tangible goods, services or the marketing, trading or distribution of commodities; or
 - b. The tested party carries out non-distribution activities in addition to the qualifying transactions unless the qualifying transactions can be adequately evaluated on a separate basis and can be reliably priced separately from the non-distribution activities.

2.2. MOST APPROPRIATE METHOD

The transactional net margin method (TNMM) is the most appropriate method to be used under the simplified and streamlined approach.

However, there may be instances (although these may be rare, as the distribution of commodities is excluded from scope) where the application of the comparable uncontrolled price (CUP) method using internal comparables could be potentially more appropriate to apply to price in-scope transactions. For those instances, for transactions within the scope of the simplified and streamlined approach, an exception is provided that allows for the CUP method using internal comparables to be used to reliably price in-scope transactions. Both the comparables and any information utilised to determine that the application of the CUP method is more appropriate must be readily available to both the tax administration and taxpayer.

2.3. DETERMINING THE RETURN UNDER THE SIMPLIFIED AND STREAMLINED APPROACH

For the purposes of the simplified and streamlined approach, return on sales is applied as the net profit indicator for the purpose of establishing pricing outcomes for in-scope transactions. A pricing matrix as below is used to price qualifying transactions. The matrix is an approximation of arm's length results presented as matrix segments according to the following factors:

- i) net operating asset intensity (OAS),
- ii) operating expense intensity (OES) and
- iii) industry groupings.

INDUSTRY GROUPING	INDUSTRY GROUPING 1	INDUSTRY GROUPING 2	INDUSTRY GROUPING 3
Factor intensity			
[A] High Net operating asset intensity (OAS)/Any Operating expense intensity (OES) >45% OAS/any level OES	3.50%	5.00%	5.50%
[B] Medium/High OAS/Any OES 30% - 44.99% OAS/any level OES	3.00%	3.75%	4.50%
[C] Medium/Low OAS/Any OES 15% - 29.99% OAS/any level OES	2.50%	3.00%	4.50%
[D] Low OAS/non-low OES <15% OAS/10% or higher OES	1.75%	2.00%	3.00%
[E] Low OAS/Low OES <15% OAES/<10% OES	1.50%	1.75%	2.25%

In order to determine the return for a tested party involved in qualifying transactions for the relevant fiscal year, a tax administration and relevant taxpayer will apply a 3-step process, as summarised below:

Step 1 - determine the relevant industry grouping(s) of the tested party from the three possible groupings (i.e. industry grouping 1, 2, 3) and identify the applicable vertical column(s) of return on sales in the pricing matrix that correspond to that industry grouping.

Step 2 - determine the relevant factor intensity classification of the tested party from the five possible classifications (i.e. factor intensity classification A, B, C, D, and E) and identify the applicable horizontal row of return on sales in the pricing matrix that corresponds to that factor intensity classification. The factor intensity classification of the tested party should be calculated based on a weighted average of the three preceding fiscal years.

Step 3 - identify the range from the pricing matrix segment that corresponds to the intersection of the industry grouping(s) and the factor intensity classification of the tested party.

The return derived from application of Step 3 will produce a range equal to the return on

sales percentage derived from the pricing matrix plus or minus 0.5%. Any point within that acceptable range will form the basis for any subsequent adjustments.

OPERATING EXPENSE CROSS-CHECK

For the purposes of the simplified and streamlined approach, an operating expense cross-check is applied as a guardrail within which the primary return on sales net profit indicator is applied. Where the application of the return on sales net profit indicator produces a result outside of the pre-defined operating expense cap-and-collar range specified in the table below, the profitability of the tested party will be adjusted.

Where the equivalent return on operating expense of the tested party exceeds the operating expense cap, the return on sales of the tested party will be adjusted downwards until it results in an equivalent return on operating expense equal to the operating expense cap.

Conversely, where the equivalent return on operating expense of the tested party falls below the operating expense collar, the return on sales of the tested party will be adjusted upwards until it results in an equivalent return on operating expense equal to the operating expense collar.

The default cap rates apply unless the tested party is located in a qualifying jurisdiction. In such cases the alternative cap rates apply.

A qualifying jurisdiction is defined as jurisdictions that are classified by the World Bank Group as low income, lower-middle income and upper-middle income jurisdictions based on the latest available World Bank Group country classifications by income level. The list of qualifying jurisdictions will be fixed prospectively, published and updated every five years.

ATAF and African Inclusive Framework members considered that the default cap rates in the above table were not appropriate for lower income countries and would lead to results that may not be an approximation of an arm's length outcome. We successfully negotiated with the Inclusive Framework for the higher alternative cap rates shown in the second column of the above table for low income, lower-middle income and upper-middle income countries. All but one African country (including non-Inclusive Framework members) will have the benefit of using the higher alternative cap rates.

DATA AVAILABILITY MECHANISM FOR QUALIFYING JURISDICTIONS

Where a tested party is located in a qualifying jurisdiction, an adjustment will be made to the return initially determined under the above pricing matrix and operating expense cross check where applicable. A relevant taxpayer in an aforementioned qualifying jurisdiction will earn an adjusted return in accordance with the following formula:

Adjusted return on sales = ROSTP + (NRAJ x OASTP) Where –

- **ROSTP** is the return on sales percentage of the tested party calculated in accordance with the above pricing matrix and the operating expense cross-check where applicable.

- **NRAJ** is the net risk adjustment percentage of the qualifying jurisdiction derived from the table below, where the applicable category is determined by reference to the sovereign credit rating of the qualifying jurisdiction of the tested party applicable on the first day of the relevant fiscal year.

- **OASTP** is the net operating asset intensity percentage of the tested party for the relevant fiscal year but will not exceed 85% for the purpose of computing the adjusted return on sales of the tested party.

OPERATING EXPENSE CAP AND COLLAR RANGE

FACTOR INTENSITY	DEFAULT CAP RATES	ALTERNATIVE CAP RATE FOR QUALIFYING JURISDICTIONS	COLLAR RATE
High OAS [A]	70%	80%	10%
Medium OAS [B] and [C]	60%	70%	
Low OAS [D] and [E]	40%	45%	