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**Assessing the Impact of Amount B**

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*KPMG practitioners discuss the challenges businesses may face when implementing the OECD's Amount B initiative.*

On February 19, 2024, the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting released a report on Amount B, the OECD's initiative to simplify and streamline the application of the arm's length principle ("ALP") to baseline marketing and distribution activities. The guidance gives jurisdictions the option to apply the Amount B approach from January 2025, either as a taxpayer safe harbor or as a mandatory rule.

As businesses begin to assess the impact of Amount B they are starting to identify unexpected outcomes and potential challenges. This article highlights some of these outcomes and challenges that businesses should consider in their response to Amount B.

## Impact of Amount B

The first step for most businesses when assessing the potential impact of Amount B is to examine the pricing matrix. The pricing matrix establishes Amount B returns that range from an operating margin ("OM") of 1.5% to 5.5%, varying by industry and the factor intensity of a distributor in respect of an in-scope transaction. This enables businesses to identify how their current transfer pricing policies or results vary from where they expect entities to fall in the matrix.

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As a second step, businesses have started to model the impact of Amount B for a handful of pilot jurisdictions. This modeling exercise can be helpful in revealing some of the implementation challenges that Amount B may pose:

- **Entity (and potentially transaction) specific results.** Amount B is applied to individual entities (or individual transactions where entities purchase goods from multiple related parties) and hence the return delivered by the Amount B matrix can vary by entity (or transaction). This may cause disruption for businesses that have regionally or globally standardized transfer pricing policies for distributors.
- **Segmentation.** Amount B can be applied to a distribution function, where this function can be segmented from other activities that are excluded from Amount B (e.g., manufacturing). This adds more complexity to the already challenging area of segmentation, including a requirement to segment operating asset data (see below). These challenges multiply when a distributor purchases goods from more than one related party.
- **Operating asset data.** The Amount B pricing matrix requires businesses to determine the operating asset intensity of a distributor. This is often data that transfer pricing departments do not have easy access to, and which they may review infrequently, if at all. When businesses have been able to access this information, many have been surprised by the significant asset balances that sit with some distributors. In an Amount B world, higher asset balances result in a higher return in the matrix; therefore, these "balance sheet surprises" push up the returns these entities would be required to earn under Amount B.
- **Operating expense to sales threshold.** Amount B is limited to entities with an operating expense to sales threshold of more than 3% and less than 20 – 30% (with the upper threshold a decision for individual tax authorities). Operating expenses exclude pass-through costs, but no additional guidance is provided on how to identify such costs. This threshold can result in distributors with material operating expenses (e.g., advertising and promotion expenses) potentially being excluded from Amount B.
- **Operating expense cross-check ("OECC") and data availability mechanism (i.e., developing country uplift).** The application of the OECC and the data availability mechanism are much less intuitive than the Amount B pricing matrix. Businesses have been surprised by the situations where the OECC does and doesn't apply, and the potential impact of the data availability mechanism, though the list of jurisdictions that will benefit from this mechanism has not yet been finalized.
- **Applicable financial accounting standards.** Amount B must be applied based on any accounting standard that is permitted as a basis for preparing financial statements in the jurisdiction where the tested party is located, or other accounting standards that are specifically permitted by the jurisdiction. This means that absent specific permission, U.S. multinationals would not be able to rely upon their U.S. Generally Accepted Accounting Principle ("U.S. GAAP") financial statements as the basis for applying Amount B outside jurisdictions where U.S. GAAP is a permitted accounting standing, such as the U.S. In situations where there are variances between accounting standards, this can make it difficult to estimate the impact of Amount B.

Different businesses will face different challenges in assessing the impact of Amount B, but it is only by lifting the lid on the calculation – at least for a handful of pilot jurisdictions – that these challenges can be identified. Though it is still early days, groups may also want to start thinking about their compliance strategy. This includes strategizing for scenarios where Amount B is enforced as a mandatory rule or safe harbor in a jurisdiction where an in-scope distributor is resident, but is not accepted by the jurisdiction of the counterparty involved in the covered transaction.

## Operational Issues

Having understood the potential impact of Amount B, businesses have started to think about how they would operationalize this new approach to setting and testing the returns for their baseline distributors. These challenges can be significant and include:

- **Narrow target operating margin.** Under the Amount B pricing matrix, an entity will need to hit a target operating margin that varies by one percentage point. For many groups, this will create operational transfer pricing challenges – and has the potential to push them to make more frequent and more significant post-year-end adjustments. Under the OECC, it is even unclear if this narrow one percentage point range will be permitted, with groups instead potentially being required to hit a fixed point specified by the OECC. This will create material additional challenges for operational transfer pricing and make post-year end transfer pricing adjustments, which not all jurisdictions permit, a virtual certainty.
- **Uncertainty about the return entities will need to achieve.** The Amount B pricing matrix is set based on prior year data. For example, for 2025, it would typically look at the average functional intensity of a distributor from 2022 to 2024. However, most businesses will only get financial data for 2024 (particularly local statutory accounting information) towards the end of 2025. This can make it difficult at the start of the year to determine the appropriate operational transfer pricing needed to allow an entity to hit the targeted return required under Amount B. Even in situations where the data may be available earlier in the year, the OECC is based on the current year operating expenses. Determining if OECC is triggered would require groups to monitor the returns on operating expenses throughout the current year.
- **Reliance on local statutory accounting information.** The Amount B report implies that, unless specifically specified, groups will need to apply Amount B based on local statutory accounting information, not U.S. GAAP accounts. These accounts are typically prepared to a slower timetable, raising more questions about data accessibility.
- **Efficient data retrieval and management.** Amount B will require businesses to access additional data to set and test the price of their baseline distributors, including historical data. This will require them to put in place efficient processes to retrieve and manage transaction-level data.

## Conclusion

Amount B is intended to provide a simplified and streamlined approach to the pricing of baseline marketing and distribution activities. Achieving that objective requires Amount B to reduce the recurring disputes between tax authorities over the pricing of routine distribution activities, which remains a laudable, if uncertain, objective. But in the meantime, businesses need to start thinking about the application of a new transfer pricing framework that will create new pressures and challenges and could apply from 2025.

When considering the operationalization of Amount B, businesses should think about opportunities for synergies. Thinking about integrating Amount B into existing Pillar Two projects, or updates to enterprise resource planning (“ERP”) systems are practical ways to make the operationalization of Amount B easier.

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