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"Taxation Where Value is Created" and the OECD/G20 Base Erosion and Profit Shifting Initiative

This article examines the concept of "taxation where value is created" and its role as a potential solution to the issues raised with regard to the OECD/G20 Base Erosion and Profit Shifting initiative.

1. "Taxation Where Value is Created": The Core of the OECD/G20 Base Erosion and Profit Shifting Initiative

Dealing with base erosion and profit shifting presupposes that it is known what this is. The concept of value creation claims to provide an answer as to where profits should be taxed and, therefore, when the tax base is being shifted. The OECD introduced value creation as the central benchmark. All of the OECD's anti-base erosion and profit shifting measures are intended to "ensure that profits are taxed where economic activities take place and value is created".[1] Consequently, "taxation where value is created" can be regarded as being at the core of the OECD Base Erosion and Profit Shifting (BEPS) initiative.

However, value creation can only function as a benchmark if it presents clear answers to the issues of allocation. In addition, if value creation becomes the ultimate overruling criterion for the allocation of taxing rights, it is necessary to understand how this deviates from the existing allocation rules, as the OECD did not intend to depart from the current international tax system,[2] the question arises whether value creation is a new idea[3] or only reformulating existing principles. This leads to the need to analyse the concept and the nature of the principle of "taxation where value is created".

2. The Nature and Concept of "Taxation Where Value is Created"

2.1. The unclear concept of value creation as an allocation factor

The concept of value creation has never been clarified with regard to the OECD/G20 BEPS initiative. Nowhere in all of the publications regarding the OECD/G20 BEPS initiative is it possible to find any explanation why this should be the underlying principle of the international allocation in respect of taxing rights. The OECD has also not tried to define the factors and the location in respect of value creation.[4]

The lack of a clear concept already reveals itself in the combination of "(real) economic activity"[5] and the "creation of value". In this context, the OECD refers to both at the same time, even though the location of the real economic activity and that of the creation of value do not necessarily coincide. It is likely that in a location where a multinational enterprise (MNE) exercises real economic activity, some value is created and even more likely that where no real economic activity takes place, there is no value creation. However, the extent of the created value is not necessarily proportional to the intensity of economic activity. A low-wage production site does not contribute much to the creation of value, despite the fact that a large number of individuals are involved in performing intense real economic activity.[6] Consequently, with regard to the question of whether a jurisdiction deserves to have some of the tax base, economic activity and value creation are tautological. However, with regard to the amount of the attributed tax base, these two factors can have different results. A lack of a hierarchy between real economic activity and value creation results in significant discretional leeway.

2.2. The function of "taxation where value is created" in the OECD/G20 BEPS initiative

One reason for the oscillating character of the new allocation standard is that focusing on value creation serves the

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1. OECD, *Explanatory Statement: OECD/G20 Base Erosion and Profit Shifting Project* para. 1 (OECD 2015). Followed by the European Union. *See*, for example, European Commission, Communication from the Commission to the European Parliament and the Council of 17 June 2015 A Fair and Efficient Corporate Tax System in the European Union: 5 Key Areas for Action pp. 10-11 COM (2015) 302 final, EU Law IBFD.
2. OECD, *supra* n. 1, at para. 8, where the OECD's task is stated to be the "renovation" and not the replacement of the existing international tax standards.
3. M. Herzfeld, *The Case against BEPS: Lessons for Tax Coordination*, 42 Fla. Tax Rev. 1, p. 42 (2017), who states that this is a "brand new standard … which had never considered the allocation of profits based on value creation". *See also* D. Stewart, '*Value Creation' Understanding Key to Transfer Pricing's Future*, 79 Tax Notes Intl. 4, p. 322 (2015).
4. Herzfeld, *supra* n. 3, at pp. 1 and 34.
5. Fundamental, *see* E.C.C.M. Kemmeren, *Principles of Origin in Tax Conventions: A Rethinking of Models*, p. 43 (Pijnenburg vormgevers.uitgevers 2001), who states that "substantial activity" means "an essential and significant part of the activity as a whole".
6. Herzfeld, *supra* n. 3, at p. 42.

following two different functions in respect of the agenda of the OECD/G20 BEPS initiative:

(1) With regard to upholding the existing international tax system, the OECD/G20 BEPS initiative is intended to identify and deal with aggressive tax planning and tax avoidance. With regard to this function, value creation has been the guiding principle of the OECD/G20 BEPS initiative in respect of Action 3, as "CFC rules generally include income that has been separated from the underlying value creation to obtain a reduction in tax".[7] Action 8-10 on transfer pricing even have the objective of "aligning transfer pricing outcomes with value creation" in their title.[8] In contrast, Action 5, which deals with harmful tax competition and focuses on intellectual property (IP) regimes, attached priority to a "substantive business requirement" vis-à-vis the value creation approach. The substantial activity requirement has been defined as essential for the acceptance of any preferential regime and has resulted in the nexus approach, which, at least, does not directly reflect the value contribution of a research and development (R&D) activity.[9] A value creation approach, which would require taxpayers to undertake a set number of significant R&D activities, was discussed, but not accepted.[10]

(2) More fundamental is the second role that the OECD attributed to value creation as an overarching principle for the justification and allocation of taxing rights. With regard to this function, the ongoing debate regarding the tax challenges of the digital economy that are addressed in Action 1[11] is of particular importance.[12] Here, the concept of value creation is not limited to the attribution of profits for the application of the existing corporate income tax, but is also a fundamental reason for the invention of new taxable items. The OECD process started from the identification of a deficit, thereby intending to protect the existing tax base against unfair tax competition and aggressive tax planning. It is somewhat paradoxical that from this starting point, based on the concept of "taxation where value is created", countries have developed new tax bases, not only protecting but also expanding their taxing rights. Countries, which, given their contribution to value creation, adopt the position that they not have the appropriate taxing rights invent new taxes. This has already happened in India and been discussed at an EU level. The main drivers of this are the discovery of the significance of the market as well as of consumer data as a new form of natural resource that can be exploited by data mining by way of monopolistic networks. In addition, if value creation results in investment shifting rather than profit shifting,[13] this could motivate countries suffering from the effects of investment shifting to introduce new taxes. The resulting defensive measures of countries affected by such new taxes are a likely consequence, which also give rise to the risk of new double taxation.

2.3. A source principle

Allocation conflicts arise between residence and source states, as well as between different residence and different source states. Value creation is a source principle, not a residence principle. It can be a principle of origin,[14] as well as of destination, depending on whether "the market" is conceived as a value adding factor with value being created by users and consumers.[15] This view, also referred to as "value realisation", is especially held by certain emerging markets, particularly China. The rationale is the following: Without customers an MNE could create goods and services, but, ultimately, it needs consumers to make an investment valuable.[16] From this perspective, value creation would permit market countries to claim a share of the tax base in proportion to production countries.

However, the jurisdiction in which the headquarters is located can also build on the value creation principle and claim a part of the tax base, not based on the residence of the headquarters, but on its contribution to the value created. The fact that MNEs operate as a single entity rather than a group of independent entities is due to the controlling power of the parent corporation. Given a value creation approach, this justifies taxation of part of the group's profits in the country of the parent, even if the (real) economic activity is exercised elsewhere.

Clear-cut answers can be expected only in the negative. It is somehow trivial, and therefore with no doubt likely to achieve consensus, that value is, possibly, not created in a tax haven. Apart from this, determining the place of value creation is very difficult.[17] If economic activity takes place

7. OECD, *Action 3 Final Report 2015 – Designing Effective Controlled Foreign Company Rules* para. 74 (OECD 2015), International Organizations' Documentation IBFD [hereinafter: the "*Action 3 Final Report* (2015)"].
8. OECD, *Action 8-10 Final Report 2015 – Aligning Transfer Pricing Outcomes with Value Creation* (OECD 2015), International Organizations' Documentation IBFD [hereinafter: the "*Action 8-10 Final Report* (2015)"]. *See also* OECD, *Action 3 Final Report* (2015), *supra* n. 7, at p. 9.
9. OECD, *Action 5 Final Report 2015 – Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance* ch. 4 II (OECD 2015), International Organizations' Documentation IBFD.
10. Id., at para. 27.
11. OECD, *Action 1 Final Report 2015 – Addressing the Tax Challenges of the Digital Economy* (OECD 2015), International Organizations' Documentation IBFD [hereinafter: "*Action 1 Final Report* (2015)"].
12. On this, *see* W. Schön, *Ten Questions about Why and How to Tax the Digitalized Economy*, 72 Bull. Intl. Tax. 4-5 (2018), Journals IBFD.
13. U. Schreiber, *Sales-Based Apportionment of Profits*, 72 Bull. Intl. Tax. 4-5 (2018), Journals IBFD.
14. S.A. Stevens, *The Duty of Countries and Enterprises to Pay Their Fair Share*, 42 Intertax 11, p. 703 (2014).
15. R.S. Avi-Yonah & H. Xu, *Evaluating BEPS: A Reconsideration of the benefits Principle and Proposal for UN Oversight*, 6 *Harv. Bus. L. Rev.* 2, p. 213 (2016).
16. China International Tax Center/International Fiscal Association (IFA) China Branch, in OECD, *Comments Received on Public Discussion Draft - BEPS Action 10: Use of Profit Splits in the Context of Global Value Chains* p. 101 (OECD 2015), available at www.oecd.org/tax/transfer-pricing/public-comments-action-10-profit-splits-global-value-chains.pdf and M. Herzfeld, *Splitting Profits with Communists*, 79 Tax Notes Intl. 6, p. 467 (2015).
17. W.F. Richter, *Taxing Intellectual Property in the Global Economy: A Plea for Regulated and Internationally Coordinated Profit Splitting*, CESifo Working Paper No. 6564, p. 2 (2017), available at www.cesifo-group.de/DocDL/cesifo1_wp6564.pdf.

in more than one jurisdiction, it is not possible to indicate that and, even more important, to what extent value is created in one jurisdiction but not in the other. Almost any location can be considered as having contributed to value creation in some way.

The lack of clear-cut answers is not surprising. Value creation as a rationale for determining the location of taxation is a concept, an idea or a principle,[18] but not a rule that can be applied without discretion. And yet, value creation is probably not more imprecise than any other principle, such as the principle of ability to pay or the source principle. Source taxation also permits very different interpretations.[19] The problem with value creation as the new guiding principle stems from the fact that it pretends to give better answers to the issues of allocation, while eventually turning out to be only a new variant of the source principle.

2.4. Does value creation only concern revenue and not justice?

As unclear as the concept is the nature of the value creation standard. Criticism has rightly been made that the OECD has invented a guiding principle without conducting any thorough analysis of its effects and without any clear theoretical foundation.[20] In other words, the standard has emerged of the blue.

Value creation started as a political idea. The question is whether the new principle only relates to tax revenue[21] and extending the discretional powers of tax administrations or whether it has a deeper justification.

This may sound cynical, but the OECD/G20 BEPS initiative suffers from an overemphasis on fairness, justice and morality, or perhaps only a vague notion of justice or injustice.[22] The active role of non-governmental organizations (NGOs), such as the Tax Justice Network (TJN),[23] media awareness and the identification of the problem with well-known MNEs, such as Apple and Amazon, has given the public the illusion of being able to understand the complex issues of international taxation and has pressurized politicians into taking action.[24] Normally, treaty law is the domain of representatives of the tax administrations involved, with the focus being on tax revenue. This time, however, politicians became involved and they were not interested in technicalities but in the great ideas of distributional justice and fairness. The idea of taxing profits where value is created served as an almost intuitive benchmark for international distributive justice. And in some countries, which appears to be especially true in Germany, politicians were, at least initially, not even aware of the consequences all of these ideas could have on the country's revenue.[25]

Apart from the recent, but superficial political debate on tax justice, the rationale behind value creation is not new. As already noted, this is a source principle and can be traced back to the benefit principle as one, if not *the* fundamental, justification for countries levying taxes.[26] The benefit principle is also a guiding principle when it comes to the international allocation of taxing rights among jurisdictions and is said to lead to inter-nation equity[27] in the sense that Musgrave and Musgrove (1972) intended.[28] If a country provides and finances public goods, which contribute to the creation of value, it has a legitimate interest in taxing the outcome.

So maybe justice is not the problem. The real problem is that not much is known regarding the effects of value creation as a factor for the allocation of taxing rights with regard to efficiency, neutrality or even practicability.

Some of these problems arise from the incoherence between the theoretical foundation and the tax base to which it is applied. It could be possible to identify a country's contribution to the creation of value due to the use of the natural or human resources, infrastructure and the legal system concerned. However, this requires for direct charges and fees, which would be measured in relation to the use of such public goods, and not in the taxation of profits.[29] Consequently, the use of public goods is neither a good justification for taxing income nor does it provide any guidance for measuring and attributing the income of an MNE to different jurisdictions. Some MNEs could make intense use of public goods but ultimately realize significant losses, such as in the ship building industry. It is also unclear as to how the corporate income tax as a tax on profits interacts with VAT or with taxes on the

18. With regard to whether this is a principle, rule or standard, *see* S.C. Morse, *Value Creation: A Standard in Search of a Process*, 72 Bull. Intl. Tax. 4-5 (2018), Journals IBFD.
19. K. Vogel & A. Rust, *Introduction*, in *Klaus Vogel on Double Taxation Conventions* 4th edn., paras. 15 and 17 (E. Reimer & A. Rust eds., Wolters Kluwer 2014); R. Rohatgi, *Basic International Taxation: Vol. 1 Principles of International Taxation* 2nd edn., p. 223 (BNA Intl. 2005); E.C.C.M. Kemmeren, *Source of Income in Globalizing Economies: Overview of the Issues and a Plea for an Origin-Based Approach*, 60 Bull. Intl. Taxn. 11, sec. 2.2. (2006), Journals IBFD; A. Becker, *The Principle of Territoriality and Corporate Income Taxation – Part 1;* 70 Bull. Intl. Taxn. 4, sec. 3.1.1. (2016), Journals IBFD; and L.U. Cavelti, C. Jaag & T.F. Rohner, *Why Corporate Taxation Should Mean Source Taxation: A Response to the OECD's Actions against Base Erosion and Profit Shifting*, 9 World Tax J. 3, sec. 2. (2017), Journals IBFD.
20. Morse, *supra* n. 18.
21. Y. Brauner, *What the BEPS?*, 16 Fla. Tax Rev. 2, p. 59 (2014).
22. Similarly sceptical, *see* P.B.W.L. Lamberts, *Fair Taxation: Truth is in the Eye of the Beholder*, 45 Intertax 2, p. 49 (2017).
23. S. Shaheen, *Battle Line Drawn between OECD and Tax Justice Network*, 23 Intl. Tax Rev. 4, p. 12 (2012).
24. With regard to the media frenzy and the opportunistic roots of the project, *see* Brauner, *supra* n. 21, at p. 112 and H.J. Ault, W. Schön & S.E. Shay, *Base Erosion and Profit Shifting: A Roadmap for Reform*, 68 Bull. Intl. Taxn. 6/7 (2014), Journals IBFD.
25. D. Piltz, *BEPS und das staatliche Interesse*, 24 Internationales Steuerrecht (IStR) 15, p. 529 (2015).
26. Stevens, *supra* n. 14, at p. 703. With regard to "group fiscal equivalence", *see* P. Dietsch & T. Rixen, *Tax Competition and Global Background Justice*, 22 J. Political Phil. 2, p. 158 (2014), in referring to U. Thielemann, *Grundsätze fairen Steuerwettbewerbs - Ein wirtschaftsethisches Plädoyer für einen Steuerleistungswettbewerb*, in *Regulierung oder Deregulierung der Finanzmärkte* p. 116 (B. Britzelmaier et al. eds., Physica-Verlag 2002). Critical of the benefit principle, *see* Avi-Yonah & Xu, *supra* n. 15, at pp. 188 and 210 and R.S. Avi-Yonah & H. Xu, *Evaluating BEPS*, 10 *Erasmus L. Rev. 1, p. 4* (2017).
27. OECD, *Action 1 Final Report* (2015), *supra* n. 11, at para. 12.
28. R.A. Musgrave & P.B. Musgrave, *Inter-Nation Equity*, in *Modern Fiscal Issues: Essays in Honor of Carl S. Shoup*, p. 71 (R.M. Bird & J.G. Head eds., U. Toronto Press 1972). *See also* recently Richter, *supra* n. 17, at p. 9.
29. W. Schön, *International Tax Coordination for a Second-Best World (Part I)*, 1 World Tax J. 1, sec. 2.2.2.1. (2009), Journals IBFD and Schön, *supra* n. 12.

exploitation of natural resources if the international allocation is based on the concept of value creation.

2.5. Adequate and sufficient to resolve the problems of the arm's length standard?

Given that value creation is not a new panacea for international tax law or in respect of base erosion and profit shifting, it should potentially be, at least, adequate and sufficient to resolve the problems of the arm's length standard.[30] Allocating taxing rights to the location of value creation could reduce manipulation by contractual arrangements. Specifically, it would limit the relevance of ownership and, therefore, could be conceived as a more economic approach to allocation. However, even a detailed analysis of value added chains would not permit the attribution of a specific amount of the profits to a given location. The outcome would be even more discretional than under contractually based dealings using the arm's length standard.

The main difference between separate entity accounting and the arm's length standard is that value creation, at least, to date, lacks any formal restrictions or thresholds. Currently, the application of the source state principle requires a certain minimum nexus to the territory of the source state.[31] The traditional concept of a permanent establishment (PE) is, primarily for the sake of administration and compliance costs, a threshold for source taxation.[32] Contracts and the ownership of assets in the existing transfer pricing have a similar function. Value creation questions such thresholds. Everything can contribute to the creation of value. The efforts made in Action 8 to provide a definition of the term "intangible"[33] can be recognized as an attempt to define a threshold. However, the width of the given definition has rightly been criticized.[34]

It can be seen as a merit of value creation that it permits a more detailed division of the tax base than the traditional, but challenged,[35] one-source approach. Specifically, it enables more countries to obtain an, albeit logically smaller, part of the taxing rights. However, it has advantages and disadvantages at the same time, as it is impossible to say, where to stop. The debate regarding the relevance of the consumer market or of raw data gathered from the behaviour of consumers provides an idea how far the value creation approach can go. In addition, if creativity is the driving force for economic growth,[36] countries that only finance education could also claim a right to tax profits, even if earned outside their borders.

The systemic flaw of separate entity accounting is that it cannot attribute the effects of integration and synergies.[37] Treating the members on an MNE as if they were independent is a fiction, which inherently ignores the economic facts and outcome of an integrated business and, therefore, the real nature of MNEs.[38] However, the concept of value creation cannot resolve this problem either. On the one hand, it casts light on the fact that the value added chains of MNEs are highly integrated. Taxing the profits of MNEs "where economic activities take place and value is created" cannot be realized without treating an MNE as a single entity, thereby reflecting the synergies of integration.[39] On the other hand, there is no factual base for the allocation of the value created by these synergies. It could, for example, be entirely attributed to the headquarters, which is responsible for the master plan of integration. However, it is far from obvious whether the jurisdiction in which the parent is located deserves to tax all of the extra profits that arise from integration,[40] as it also requires the group members and their interaction to produce this profit. This indicates the splitting up of the profits arising from integration among all of the group members.[41] The concept of value creation, therefore, does not help to define the adequate portion for each member of the group.

The logical answer to the finding that an exact split and attribution of value creation is impossible is formulary apportionment,[42] as has been, with unpredictable political success, proposed in the EU directive for a Common Consolidated Corporate Tax Base (CCCTB).[43] The increasing

30. In detail, *see* R.S. Collier & J.L. Andrus, *Transfer Pricing and the Arm's Length Principle after BEPS*, chs. 7 and 8 (Oxford U. Press 2017) and J.L. Andrus & P. Oosterhuis, *Transfer Pricing after BEPS: Where Are We and Where Should We Be Going?*, 95 Taxes: Tax Mag. 3, p. 75 (2017).
31. Stevens, *supra* n. 14, at p. 703.
32. E. Reimer, *Art. 5: Permanent Establishment*, in Reimer & Rust, *supra* n. 19, at para. 2.
33. OECD, *Action 8-10 Final Report* (2015), *supra* n. 8, at p. 67.
34. X. Ditz, R. Pinkernell & C. Quilitzsch, *BEPS-Reformvorschläge zu Lizenzgebühren und Verrechnungspreisen bei immateriellen Wirtschaftsgütern aus Sicht der Beratungspraxis*, 23 IStR 2, p. 49 (2014); M. Olbert & C. Spengel, *International Taxation in the Digital Economy: Challenge accepted?*, 9 World Tax J. 1, sec. 3.1.3. (2017), Journals IBFD; and J. Wittendorf, *BEPS Actions 8-10: Birth of a New Arm's-Length Principle*, 81 Tax Notes Intl. 4, p. 344 (2016).
35. Schön, *supra* n. 29, at sec. 1.2.
36. J.A. Schumpeter, *Capitalism, Socialism and Democracy*, ch. VII (Routledge 2003) and R. Florida, *The Rise of the Creative Class*, p. 4 (Basic Books 2002).
37. M.A. Kane, *Transfer Pricing, Integration and Synergy Intangibles: A Consensus Approach to the Arm's Length Standard*, 6 Word Tax J. 3, sec. 1. (2014), Journals IBFD.
38. *See* R.S. Avi-Yonah, *The Rise and Fall of Arm's Length: A Study in the Evolution of U.S. International Taxation*, 15 Va. Tax Rev. 1 , p. 89 (1995) and *Between Formulary Apportionment and the OECD Guidelines: A Proposal for Reconciliation*, 2 World Tax J. 1, sec. 2. (2010), Journals IBFD; R.S. Avi-Yonah & I. Benshalom, *Formulary Apportionment – Myths and Prospects*, 3 World Tax J. 3, sec. 2.2. (2011), Journals IBFD; S. Greil, *The Dealing at Arm's Length Fallacy: A Way Forward to a Formula-Based Transactional Profit Split?*, 45 Intertax 10, p. 624 (2017); G. Rectenwald, *A Proposed Framework for Resolving the Transfer Pricing Problem: Allocating the Tax Base of Multinational Entities on Real Economic Indicators of Benefit and Burden*, 22 Duke J. Comp. & Intl. L. 3, p. 427 (2012); and H. Luckhaupt, M. Overesch & U. Schreiber, *The OECD Approach to Transfer Pricing: A Critical Assessment and Proposal*, in *Fundamentals of International Transfer Pricing in Law and Economics* p. 100 (W. Schön & K.A. Konrad eds., Springer 2012).
39. Avi-Yonah & Xu, *supra* n. 15, at p. 209.
40. Greil, *supra* n. 38, at p. 628, who advocates the full allocation of the residual profit to the sales-oriented companies of the group.
41. *See* Richter, *supra* n. 17, at pp. 21 and 26 for the residual profit.
42. R.S. Avi-Yonah, K.A. Clausing & M.C. Durst, *Allocating Business Profits for Tax Purposes: A Proposal to Adopt a Formulary Profit Split*, 9 Fla. Tax Rev. 5, p. 497 (2009) and R.S. Avi-Yonah, *A Proposal for Unitary Taxation and Formulary Apportionment to Tax Multinational Enterprises*, in *Global Tax Governance* p. 289 (P. Dietsch & T. Rixen eds., ecpr press 2016).
43. European Commission, Proposal for a Council Directive of 25 October 2016 on a Common Corporate Tax Base, COM (2016) 685 final, EU Law IBFD [hereinafter: the "Proposed CCCTB Directive (2016)"].

importance of functions in the transfer pricing regulations[44] also indicates this direction. However, the OECD decided not to endorse a conceptual shift to formulary apportionment,[45] in insisting that value creation only modifies the traditional contract-based transfer price system. Action 8-10 does not propose replacing transfer pricing and the arm's length standard with value creation, but aligning the outcomes.[46] And its function is of a corrective nature. It is apparently supposed to be a method for countering abusive constructions and not as an independent new standard.

The result is indecision with the OECD confronting the international tax community with two different concepts at the same time. The flaws of the existing transfer price methods, which are already known, may be further burdened with flaws of the concept of value creation, of which there is only currently a limited awareness. Such a combination would give better results only if the arm's length principle could be considered to be an indirect proxy for taxation where value is created,[47] which would sometimes have to be corrected by direct observation of the created value. However, at least historically, this has not been the purpose of the arm's length standard, which is intended to realize market neutrality between integrated and non-integrated businesses, but not necessarily in accordance with value creation.

The mixture of concepts is unlike to lead to a consistent result, the more so as Action 8-10 only focuses only on some aspects of transfer pricing and concentrates on intangibles, the contractual allocations of risks and over-capitalization. It is unclear as to how value creation affects other aspects of transfer pricing.

3. Procedural Solutions: The Need to Reduce Legal Uncertainty

Traditional transfer pricing is far from perfect and does not give rise to predictable results. However, transfer pricing rules have been established for a long period of time[48] and case-based experience helps to resolve controversies. All of this is lacking with regard to the concept of value creation. Value creation also deliberately departs from the stable lines of the contractual basis in respect of transfer pricing. This results in more interactive bargaining and negotiation between MNEs and tax authorities. If value creation permits more jurisdictions to participate in the tax base, this necessarily reduces the part of the tax base available to each participant and increases the risk of double taxation. The mixture of concepts, therefore, adds to insecurity.[49]

Standardized reporting of value added chains as envisaged in country-by-country (CbC) reporting as proposed in Action 13 could reduce double taxation due to different information regarding the facts of a case.[50] However, the greater risk of double taxation rather arises as a result of the different evaluation of these facts.[51]

If the uncertainty is not purposely used to reduce the profit shifting activities of MNEs, there is a need for procedures to provide taxpayers with guidance or, at least, to resolve disputes and avoid the subsequent double taxation. In the long run, the international tax community will probably develop a set of rules to produce predictable results, even under a value creation standard. However, in the meantime, procedures are likely to become all important. If the underlying substantive law is unclear and inconsistent, taxpayers should be able to depend on procedures and, at least, being aware of inconsistent results in advance, as well as on dispute resolution mechanisms, as set out in Action 14.[52]

Morse (2018) has proposed a "value creation dispute resolution forum"[53] as a procedure to determine and clarify the meaning of value creation. The establishment of such a forum, to which all countries that are somehow involved according to broad standing rules have access, is consistent with the multilateral nature of integrated value added chains and the necessarily holistic view on the whole business. Such a forum could be conceptualized as a clearing system, especially if it applied to a fixed tax base determined by uniform rules, as Morse (2018) suggests. Neither the arm's length nor the value creation principles provide guidance as to how to allocate the residual profit of integration. Instead of a formulary apportionment with pre-set factors, an apportionment would be determined by free negotiation within the forum. Such an open negotiation procedure could prevent manipulation and factor shifting. However, the procedure would not provide better insight[54] into the value creation standard, as an analysis

44. *See* OECD, *Action 8-10 Final Report* (2015), *supra* n. 8, at para. 6.34 regarding development, enhancement, maintenance, protection, and exploitation (DEMPE functions).
45. OECD, *Action Plan on Base Erosion and Profit Shifting* p. 14 (OECD 2013), International Organizations' Documentation IBFD. Given that the functional and neutrality effects of formulary apportionment are not, to date, well understood (*see*, for example, J.R. Hines, *Income Misattribution under Formula Apportionment,* 54 Eur. Econ. Rev. 1, p. 108 (2009), this would appear to be a wise decision.
46. OECD, *Action 8-10 Final Report* (2015), *supra* n. 8, at p. 9.
47. P. Hofmann & N. Riedel, *Transfer Pricing Laws for Developing Countries*, 72 Bull. Intl. Tax. 4-5 (2018), Journals IBFD.
48. Greil, *supra* n. 38, at p. 629.
49. Greil, *supra* n. 38, at p. 625; M. Herzfeld, *Will the OECD's Pragmatic Fudge Save Transfer Pricing*, 83 Tax Notes Intl. 5, p. 360 (2016); and Ditz, Pinkernell & Quilitzsch, *supra* n. 34, at p. 50.
50. OECD, *Action 13 Final Report 2015 – Transfer Pricing Documentation and Country-by-Country Reporting* (OECD 2015), International Organizations' Documentation IBFD.
51. H.J. Ault, *Some Reflections on the OECD and the Sources of International Tax Principles*, 70 Tax Notes Intl. 12, p. 1200 (2013) and M.A. Grau Ruiz, *Country-by-Country Reporting: The Primary Concerns Raised by a Dynamic Approach*, 68 Bull. Intl. Taxn. 10, sec. 3.2.3.1. (2014), Journals IBFD.
52. OECD, *Action 14 Final Report 2015 – Making Dispute Resolution Mechanisms More Effective* (OECD 2015), International Organizations' Documentation IBFD.
53. Morse, *supra* n. 18.
54. Consequently, making this process open to the public would not provide guidance in other cases. In addition, in such a forum procedure, details of the value added chains of MNEs could not discussed in public so as not to reveal sensitive information on the business model of the MNEs in question. The purpose of the transparency of the procedure would be either control or participation. As public participation would contribute little to the result of such a forum procedure, it would not outweigh the significant disadvantage of potentially revealing business secrets, especially if the negotiating process, and not only its result, were to be made available to the public.

of the value added chains would not answer the question as to which jurisdiction could participate and up to what extent in the relevant profits generated, given the interaction of the group members.

4. Conclusions

Given its dominance, the concept of value creation as an allocation principle appears not only in the OECD/G20 BEPS initiative, but also, without further reflection, at an EU level,[55] the chance that it will suddenly disappear from the international taxation agenda is small. Value creation could be an intermediate step towards formula apportionment.[56] However, even if the combination of the classical arm's length standard and the new, but vague, concept of value creation would increase uncertainty and give rise to international tax conflicts, a political consensus on a formula in the foreseeable future appears to be unrealistic.[57] This situation requires further scholarly analysis of the effects of the value creation standard, on the one hand, and for set rules to define its content and application by the OECD, on the other.

55. *See* European Commission, COM (2015) 302 final, *supra* n. 1.
56. *See* Greil, *supra* n. 38, at p. 627.
57. Even within the European Union the chances of this happening are limited. The European Commission has modified its initial proposal for a formulary apportionment within the CCCTB (*see* European Commission, Proposal for a council directive of 16 March 2011 on a Common Consolidated Corporate Tax Base, COM (2011) 121, EU Law IBFD) into a two-step approach (*see* European Commission, Proposed CCCTB Directive (2016), *supra* n. 43), as it did not wish to jeopardize the harmonization of the tax base as a result of the reluctance of the Member States to agree on a formula.