Response: OECD Regulated Financial Services Exclusion (Pillar One – Amount A). May 20th, 2022.

Introduction

We are grateful for the opportunity to respond to the OECD's consultation regarding *Tax Challenges Arising from Digitalisation – Report on Pillar One Blueprint.*

The World Federation of Exchanges (WFE) is the global trade association for regulated exchanges and clearing houses. We represent the operators over 250 market infrastructures, spread across the Asia-Pacific region (~37%), EMEA (~43%) and the Americas (~20%), with everything from local entities in emerging markets to groups based in major financial centres. Collectively, member exchanges trade some $95 trillion a year; while the 50 distinct CCP clearing services (both vertically integrated and stand-alone) collectively ensure that traders put up $1 trillion of resources to back their risk positions.

With extensive experience of developing and enforcing high standards of conduct, WFE members support an orderly, secure, fair and transparent environment for all sorts of investors and companies wishing to invest, raise capital and manage financial risk.

We seek outcomes that maximise financial stability, consumer confidence and economic growth. We also engage with policy makers and regulators in an open, collaborative way, reflecting the central, public role that exchanges and CCPs play an internationally integrated financial system.

If you have any further questions, or wish to follow-up on our contribution, the WFE remains at your disposal. Please contact:

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Response

The WFE supports the efforts of the OECD and the G20 to understand digital transformation and to develop and implement a resilient framework that fosters a positive and inclusive global economy and society. We believe that global tax principles should be responsive to changing economic patterns and business models, while being supportive of healthy risk management and capital formation. We support harmonisation of digital taxation led by international standard-setters.

The WFE is, however, concerned that while the current drafting of the proposals continues to offer an exemption to regulated financial services it would (in our view, inappropriately) capture the most highly regulated sector, namely market infrastructure (namely exchanges, central counterparties [CCPs] and central securities depositories [CSDs]), as the sector is not currently attributed a specific exemption. This concern further arises from the fact that specific exemptions in the draft text are made only for 'banking', 'asset management' and 'insurance'. We assume it is not the intention to capture some parts of regulated financial services and not others when the same principles apply to their use of digital channels to facilitate business. Any taxation of market infrastructure would in any case indirectly affect all those who make use of that infrastructure, including those currently identified as exempt, by pushing up costs.

We encourage the OECD to maintain a level playing field for market infrastructures (MI) vis-à-vis other types of financial service provision. We therefore propose that an MI exemption be linked to the MI being registered, regulated, authorised or supervised in a country that is a member of IOSCO or (relevant for CCPs) one that has adopted the Principles for Financial Market Infrastructures[1].

We accordingly also suggest that the OECD consider using the following wording for the exemption of MI as: *"entities that are registered, regulated, authorised or supervised in a jurisdiction, or are recognised as not needing to be registered, regulated, authorised or supervised by virtue of falling outside the requirement to be so[2], or the assets in respect of which it carries on its activities expressly fall outside the requirement to be so registered, regulated, authorised or supervised."*

The WFE believes that the rationales previously proposed by the OECD for the exemptions of those three financial services sectors mentioned above are equally applicable to market infrastructure that is regulated and required to maintain appropriate resources to back their business[3]. For example, the defining characteristic of the proposed exemptions as stated in the OECD Consultation, yet also applicable to MI, is that exempt firms are subject to some form of capital adequacy requirements, which reflect the risks taken on and borne by the firm. The OECD states in its paper that it is this regulatory driver that generally helps to align the location of profits with the market. Exchanges, clearing houses and CSDs registered, regulated, authorised or supervised in a country that is a

[1] PFMI – CPMI-IOSCO, April 2012

[2] Please note that, where a piece of market infrastructure offers its services into another jurisdiction, it will not necessarily be authorised in that 'destination' jurisdiction, relying instead on cross-border arrangements between the respective regulatory regimes that may include exemption from host-country supervision or other procedures. The existence of home-country supervision remains crucial. Similarly, some infrastructure serves markets that are specifically carved out of financial-services legislation, notably in relation to spot FX and commodities. Such entities otherwise operate exactly like authorised MI and should be treated as such.

[3] For a general description of the role of such entities, please see 'Market infrastructures and market integrity: A post-crisis journey and a vision for the future', Oliver Wyman and WFE, 2018, eg, Pg. 41

member of IOSCO or (relevant for CCPs) one that has adopted the Principles for Financial Market Infrastructures are also subject to capital adequacy requirements along with organisational, conduct of business and other prudential requirements.

Moreover, regulated market infrastructure is predominantly *not* directly consumer-facing but rather operates on the basis of intermediation by wholesale market actors – notably dealers and clearing members, asset managers, settlement banks, and custodians. Thus, a retail client in the country of 'Ruritania' wishing to place, say, an order relating to shares on the stock exchange of another country, 'Sylvania', will pay for brokerage services in their home country (Ruritania), while it is that broker that interacts with the Sylvanian stock exchange and incurs charges for the services it selects, ie, execution and, if desired, data feeds.

However, it ought to be noted that not all trading-platform services necessarily operate on the same basis as the established market infrastructure we described above. For example, some online platforms (eg some of those that facilitate trading in digital assets) may operate in an automated fashion (and on a cross-border basis), without the same sort, or any, of the human oversight earlier described, and without the same regulatory compliance and high governance and operating standards. Furthermore, they will often directly target retail participation. For this reason, our proposed exemption for market infrastructure is framed in terms of those entities that are either authorised for a specific purpose in accordance with financial services regulation or specifically exempted from it.

We should emphasise that the WFE welcomes well-designed international efforts to create a fair and coherent system of taxation. However, the draft proposals may unfairly capture a sector which represents national critical infrastructure – operating for the benefit of their local economies and also overseas participants – and which is not associated with the attributes of the type of entities which these proposals appear to be seeking to capture. Should MIs be captured, there may ultimately be negative unintended consequences resulting from the imposition of such a tax, imperilling the work of MI in their role of enabling companies to raise funding and to hedge risk. To lessen or inhibit the role of MI, via the implementation of the tax, and the availability of financial products and services to companies, appears counterintuitive, especially when compared with those sectors provided with a specific exemption. It is generally accepted that market-based finance has an important role to play in the economy and society, with some parts of the world actively seeking a much larger role for capital markets[4]. This is something which is of even greater importance in light of the economic effects of the pandemic of the past two years[5] .

We welcome the opportunity to comment on the proposal and remain at your disposal should you have any questions.

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[4] Primary and secondary equity markets in the EU Final report, Oxera/European Commission, November 2020

[5] Companies have raised more capital in 2020 than ever before, The Economist, December 2020