

IRS to Adopt Simplified Transfer Pricing Rules for Distributors



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1. Introduction

Starting in 2025, the Internal Revenue Service (IRS) may allow taxpayers rely on the Streamlined and Simplified Approach (SSA) which follows the OECD's Amount B simplification rules^[3], significantly impacting transfer pricing for baseline marketing and distribution activities within the United States. Amount B provides a standardized, simplified framework for determining arm's-length returns for simple distribution functions, reducing the complexity and compliance burden associated with traditional benchmarking analyses. By utilizing pre-defined pricing matrices and simplifying the application of the arm's-length standard, the SSA aims to provide increased tax certainty, decrease compliance cost, and limit transfer pricing disputes for both tax authorities and taxpayers.

The SSA offers significant advantages to foreign groups operating in the U.S. Subsidiaries performing routine distribution functions, typically with limited risk and complexity, can now utilize this simplified method to determine their transfer pricing. This reduces the need for extensive benchmarking, leading to lower compliance costs and a more predictable tax environment.

Despite its potential benefits, the adoption of the SSA faces uncertainty due to its reliance on elements of the OECD's Inclusive Framework^[4], which the current Trump administration opposed. Consequently, multinational companies operating in the United States considering the SSA, and its simplified documentation requirement, must remain cautious and await the current administration's stance on this alternative methodological approach.

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^[3] Amount B is an integral part of the Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy agreed by the OECD/G20 Inclusive Framework on BEPS in October 2021. It introduces a simplified and streamlined approach for applying the arm's length principle to in-country baseline marketing and distribution activities, focusing on the needs of low-capacity jurisdictions.

^[4] The OECD's Inclusive Framework on Base Erosion and Profit Shifting (BEPS) is a project involving over 140 countries and jurisdictions collaborating to address tax avoidance by multinational enterprises. It aims to modernize international tax rules to reflect the digitalized and globalized economy. The framework's core is the two-pillar solution: Pillar One focuses on reallocating taxing rights to market jurisdictions where consumers are located, particularly for large digital companies, and Pillar Two introduces a global minimum corporate tax rate of 15% to prevent a "race to the bottom." Within Pillar One, "Amount B" provides a simplified and streamlined approach to determine arm's length returns for baseline marketing and distribution activities, aiming to reduce disputes and increase tax certainty.

2. Notice 2025-04

On December 18, 2024, the IRS issued Notice 2025-04 (Notice), announcing the planned implementation of the SSA into Section 482 of the Internal Revenue Code (Section 482) which governs the valuation of intercompany transactions for tax purposes. Specifically, this notice signals the U.S. Department of Treasury (Treasury) and IRS's intent to introduce the SSA as a transfer pricing method for qualifying distribution activities for tax years starting January 1, 2025. The forthcoming regulations are expected to closely align with the OECD February 24 Amount B Report (OECD Report) [5] which has been already incorporated into the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Authorities (OECD Guidelines)[6] which are followed as transfer pricing technical standard by most countries around the world.

The Notice provides crucial U.S. specific guidance on election procedures and documentation requirements however until formal regulations are released, taxpayers cannot rely on the application of the SAA. The initial implementation will follow Option 1 of the OECD Report, requiring taxpayers to actively elect to apply the SSA as a sort of safe harbor measure. However, the Treasury and IRS are also evaluating the possibility of allowing the IRS to apply the SSA, under Option 2, even without taxpayer election, potentially during audits.

Also, the Notice details the election process for taxpayers wishing to utilize the SSA. This involves submitting a statement with the original tax return, specifying the transactions to which the SSA will be applied and providing other required information. While the SSA currently applies on a transaction-by-transaction and year-by-year basis, the Treasury and IRS are exploring alternative election methods. Furthermore, the notice outlines specific documentation requirements for SSA compliance, which replace, but partially overlap with, those found in existing regulations under Section 6662(e)[7].

The SSA's relevance for U.S. taxpayers extends beyond the release of the Notice. Even if it is withdrawn, the SSA's adhesion to the Amount B included in the OECD Guidelines ensures its potential adoption by other jurisdictions. This international recognition gives the SSA practical relevance, particularly in Advance Pricing Agreements (APAs) and Mutual Agreement Procedures (MAPs). Whether formally adopted by the IRS or not, the SSA will likely play a role in negotiations involving routine distribution, providing a benchmark and potential leverage point.

3. OECD BEPS

The OECD's work to combat Base Erosion and Profit Shifting (BEPS) began in earnest with the 2015 launch of its initial BEPS Action Plan[8]. This comprehensive plan outlined 15 key actions designed to address tax avoidance strategies used by multinational enterprises, focusing on areas like transfer pricing, hybrid mismatches, and harmful tax practices. The goal was to modernize international tax rules, ensuring that profits are taxed where economic activities occur and value is created, thus preventing the artificial shifting of profits to low-tax jurisdictions.

[5] OECD Pillar One – Amount B Report published in February 19, 2024.

[6] Added as an annex to Chapter IV.

[7] Including the transfer pricing documentation to be prepared according to the requirements under Treas. Reg. 1.6662-6(d).

[8] The OECD and G20 published final BEPS (Base Erosion and Profit Shifting) reports and an explanatory statement on October 5, 2015, detailing the consensus recommendations resulting from the OECD's BEPS project, which began with a 15-action plan in July 2013.

Building upon the foundation of the original BEPS Action Plan, the OECD developed the two-pillar solution to address the challenges of the digitalized economy. Pillar One seeks to reallocate taxing rights to market jurisdictions, particularly for large multinational enterprises with significant digital presence, ensuring they pay taxes where their consumers are located. Pillar Two introduces a global minimum corporate tax rate of 15%, aiming to eliminate tax competition and ensure a baseline level of taxation for multinational profits. These pillars represent a significant shift in international tax norms, aiming to create a fairer and more stable tax environment.

The adoption of the two-pillar solution is progressing, albeit with varying degrees of success. Pillar Two has seen more widespread adoption, with numerous countries implementing or planning to implement the global minimum tax. However, Pillar One faces greater challenges, particularly concerning its implementation timeline and the complexities of reallocating taxing rights. While significant political support exists, negotiations and implementation details are ongoing, and reaching a global consensus remains a complex undertaking.



The U.S. has expressed a complex and evolving stance towards the OECD's two-pillar solution. While generally supportive of international efforts to combat BEPS, the U.S. has shown significant reservations regarding Pillar One, particularly concerning the reallocation of taxing rights. The U.S. has emphasized that any global tax agreement must not unfairly target U.S. companies and has expressed concerns about the complexity and implementation challenges of Pillar One. Regarding Pillar Two, while in essence the U.S. supports the goals of Pillar Two, its implementation within the U.S. faces significant domestic challenges. Notably, the U.S. has shown a willingness to engage with and support the Amount B aspect of Pillar One, indicating that this simplified transfer pricing approach is the only measure from the two-pillar solution that the U.S. is currently prepared to actively support.

More recently, the Trump administration has taken a clear stance against the OECD's two-pillar solution. Through a memorandum directed to the Treasury^[9], the administration has signaled its withdrawal of U.S. commitments to the OECD framework, asserting that it holds "no force or effect in the United States" without congressional enactment. The administration has also directed the Treasury to scrutinize foreign tax regimes for discriminatory practices against U.S. businesses and to consider countermeasures, especially targeting the Undertaxed Profits Rule (UTPR) and Digital Services Taxes (DSTs).

[9] Memorandum issued on January 20, 2025 instructing the Treasury Secretary to notify the OECD that any commitments made by the prior Administration with respect to the Global Tax Deal have no force or effect within the United States absent an act by Congress adopting the relevant provisions of the Global Tax Deal.

4. Amount B Methodological Approach^[10]

As indicated, the Treasury and the IRS expect that the proposed regulations will not deviate significantly from the OECD Report. Therefore, the SSA to be introduced to Section 482 is expected to mirror the Amount B rules.

The core strength of Amount B lies in its methodological framework, which leverages existing, widely accepted transfer pricing principles. It builds upon the Transactional Net Margin Method (TNMM) equivalent to the Comparable Profits Method (CPM) under the U.S. Regulations^[11], by providing a standardized profitability range based on return on sales (ROS). The standardized ROS matrix, adjusted for industry and geographical factors, offers a practical and consistent way to determine arm's length results, reducing the need for complex, fact-intensive benchmarking analysis.

Amount B's application involves two key steps: Step 1, determining if the tested party's activities fall within the scope of baseline marketing and distribution; and Step 2, applying the standardized pricing framework to qualifying transactions. The procedure for its application is summarized below^[12]:

Step 1: Scoping

- **Step 1.1. Identify qualifying transactions**

The delineation of the qualifying transaction should be undertaken in accordance with Chapter I of the OECD Guidelines.

The qualifying transactions include: i) Buy-sell marketing and distribution transactions for wholesale distribution of tangible goods to unrelated parties; ii) Sales agency and commissionaire transactions where the agent or commissionaire contributes to wholesale distribution of tangible goods to unrelated parties.

- **Step 1.2. Apply qualitative and quantitative scoping criteria**

Qualitative scoping criteria

A qualifying transaction must be economically relevant meaning that it can be reliably priced using a one-sided transfer pricing method, with the distributor, sales agent or commissionaire being the tested party. The tested party should not: i) own unique and valuable intangibles; and ii) assume economically significant risks.

Excluded transactions are: i) Distribution of services; ii) Distribution of commodities; iii) Distribution of digital goods; iv) Distribution of retail sales above de minimis threshold (more than 20% of the total net revenue); and, v) Non-distribution activities such as manufacturing, R&D and procurement, unless those non-distribution activities can be reliably segmented and separately priced using existing guidance in the OECD Guidelines.

[10] Source: www.oecd.org/en/topics/sub-issues/transfer-pricing/pillar-one-amount-b.html

[11] The Notice states "The SSA is similar to the comparable profits method under Treasury Regulation sections 1.482-3(a)(4), 1.482-5, and 1.482-9(a)(5) and (f) (referred to in the Report as the transactional net margin method as that method is known in the Guidelines)..., the SSA determines a return based on comparables and is sensitive to material factual differences between the comparables and tested parties".

[12] According to the fact sheets providing a high-level review of the mechanics for its application including examples.

Quantitative scoping criteria

The tested party should not incur annual Operating Expenses lower than 3% or greater than upper bound of between 20% to 30% of its Net Revenues. Notice that Jurisdictions can choose the upper bound of this criterion between 20% to 30%.

The Operating Expense Intensity (OES) is calculated on three-year weighted average basis.

Step 2: Pricing Framework

• **Step 2.1. Pricing Matrix**

Step 2.1.1. Determine the relevant industry grouping

Determine the relevant industry grouping based on the products being distributed by the tested party.

Step 2.1.2. Determine the relevant factor intensity classification

Factor intensity classification is determined using the OES ratio as calculated in Step 1.2 and the Net Operating Asset intensity (OAS). Similarly, the OAS ratio is calculated on a three-year weighted average basis.

Step 2.1.3. Identify the range from the pricing matrix segment

Using the information from Steps 2.1.1 and 2.1.2, the corresponding range from the predetermined pricing matrix can be identified. As shown in the following example, if the applicable industry grouping is 2 and the factor intensity classification is C, the ROS is 3.0%.

Figure 1: Pricing Matrix of Amount B^[13]

Industry Grouping	Industry Grouping 1	Industry Grouping 2	Industry Grouping 3
Factor Intensity			
(A) OAS 45% or more, any level of OES	3.50%	5.00%	5.50%
(B) OAS 30% to 44.99%, any level of OES	3.00%	3.75%	4.50%
(C) OAS 15% to 29.99%, any level of OES	2.50%	3.00%	4.50%
(D) OAS less than 15%, OES 10% or more	1.75%	2.00%	3.00%
(E) OAS less than 15%, OES less than 10%	1.50%	1.75%	2.25%

Since the pricing matrix produces a range of $\pm 0.5\%$, for this example, a return on sales between 2.5% to 3.5% would be acceptable for demonstrating compliance with Step 2.1.3.

^[13] From the Amount B fact sheets Step 2-1-3.

- **Step 2.2: Operating Expense Cross-Check (OECC)**

Step 2.2.1. Compute the equivalent return on operating expense

OECC applies after Step 2.1 as a corroborative check and computes an equivalent Return on Operating Expense (ROE). For this purpose, the Operating Expense of the current year (Year X) is used.

Step 2.2.2. Determine the applicable cap-and-collar rates

Cap rates are determined using the factor intensity classification as calculated in Step 2.1.2 and the jurisdiction where the tested party is located. Alternative cap rates apply for qualifying jurisdictions. In the following example, the factor intensity classification of the tested party is “C” and the jurisdiction where the tested party is located is a qualifying jurisdiction, therefore the cap rate is 70%.

Figure 2: OECC Example^[14]

Factor intensity	Operating expense cap-and-collar range		Collar rate
	Default cap rates	Alternative cap rates for qualifying jurisdictions	
High OAS (A)	70%	80%	10%
Medium OAS (B+C)	60%	70%	
Low OAS (D+E)	40%	45%	

Step 2.2.3. Compare the equivalent return on operating expense against the cap and collar and make an adjustment if cap or collar are triggered

If the equivalent ROE determined in Step 2.2.1 exceeds the cap determined in Step 2.2.2 or falls below the collar, the ROS will be adjusted under the OECC. The adjusted ROS under OECC can be derived as shown below:

Figure 3: Adjusted ROS Under OECC^[15]



As example, if the Net Revenue of a tested party is 300 and the Operating Expense of that party is 15 in year X, and assuming the equivalent ROE as calculated in Step 2.2.1 exceeds a cap rate of 70% as determined in Step 2.2.2, the adjusted ROS under the OECC is 3.5% $((15 \times 70\%) / 300)$.

[14] From the Amount B fact sheets Step 2-2-2.

[15] From the Amount B fact sheets Step 2-2-3.

- **Step 2.3. Data availability Mechanism (DAM)**

Step 2.3.1. Check the applicability of DAM

The DAM allows for upward adjustments to the pricing matrix ROS. This mechanism addresses situations where insufficient global data is available to validate the matrix for a tested party in a jurisdiction deemed 'higher risk'. DAM applies after Step 2.1 and 2.2 when the jurisdiction when the tested party is located in a qualifying jurisdiction.

Step 2.3.2. Calculate the adjusted return on sales

Where the tested party is located in a qualifying jurisdiction as determined under step 2.3.1, an upward adjustment will be made to the return determined. The adjusted ROS under DAM can be derived as shown below:

Figure 4: Adjusted ROS Under DAM^[16]



The net risk adjustment percentage is determined by reference to the sovereign credit rating of the qualifying jurisdiction. For example, if the ROS calculated under Step 2.1 and 2.2 is 3.0%, the sovereign credit rating of the jurisdiction where the tested party is located is B, and the OAS of the tested party calculated in step 2.1.2 is 30%, then the adjusted ROS under DAM is 4.14% (3% + (3.8% x 30%)). It should be noted that the OAS for the purpose of DAM calculation is capped at 85%.

5. Conclusion

By introducing a standardized, simplified approach to determining arm's length remuneration for baseline marketing and distribution activities, Amount B aims to reduce complexity and enhance tax certainty.

U.S. taxpayers could realize significant benefits from integrating these standardized rules, via the adoption of the SSA. The anticipated benefits, including decreased administrative burdens, lower compliance costs, and fewer disputes with tax authorities, are substantial. However, the inherent rigidity of Amount B raises concerns. Its standardized approach may struggle to capture the nuances of diverse business models and unique market conditions, potentially leading to inaccurate arm's length determinations. This could, in turn, trigger disputes over scope and application, and the reliance on a fixed ROS range may not accurately reflect the specific risks and functions of individual entities, potentially resulting in unfair tax outcomes. The reduced flexibility also limits taxpayers' ability to demonstrate unique economic circumstances, increasing the risk of higher tax liabilities or double taxation.

[16] From the Amount B fact sheets Step 2-2-3.

The future of Amount B's formal adoption in the U.S. remains shrouded in uncertainty. The current administration's evolving stance towards the OECD's international tax recommendations, particularly Pillar One and Pillar Two, introduces significant unpredictability. With potential shifts in government policy, the precise application of Amount B in US regulations by 2025 is subject to change.

Regardless of its formal regulatory status in the US, Amount B will undeniably impact transfer pricing practices. Its simplified approach will likely become a key benchmark in APAs and MAPs, especially those involving distribution activities with foreign tax authorities. This de facto standard will influence transfer pricing discussions and international tax dispute resolution, even if formal US adoption is delayed.

