


+ Seminar G: IFA/OECD

BEPS 2015 – The State of the Art and its impact on international and domestic legislation

Participants:

| | |
|---------------------------|--|
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The Timeline of BEPS:

- 2012 G20 sees „need to prevent base erosion and profit shifting“
- 2013 OECD issues „BEPS Report“ and „BEPS Action Plan“ naming 15 „Action Items“ to be delivered until December 2015
- 2014 Discussion Drafts and Deliverables
Involvement of developing countries
-  2015 Discussion Drafts and Deliverables
Ad hoc group on the Multilateral Instrument
Approval of final BEPS package by OECD and G20 (October)
- 2016 Start of Implementation

BEPS Action Plan: Where do we stand?

- 1 Digital economy
- 2 Hybrid arrangements
- 3 Strengthening CFC rules
- 4 Interest deductions
- 5 Harmful tax practices
- 6 Prevent treaty abuse
- 7 Avoidance of PE status
- 8-10 Transfer Pricing

BEPS Action Plan: Where do we stand?

- 11 Improving BEPS analysis
- 12 Mandatory disclosure
- 13 CbC Reporting / TP Documentation
- 14 Effective dispute resolution
- 15 Multilateral Instrument



BEPS: A coherent framework?

Allocation of taxing rights under BEPS:


- No fundamental change of source/residence rules
- Preventing unintended double non-taxation of business profits
- Alignment of taxation with value creation/economic substance



Coordinated approach on a global level:

- Coordinated changes to treaties and domestic legislation
- Standardised documentation and increased transparency
- International exchange of information
- Certainty and predictability for business

Setting

- Introduction
- BEPS: The bigger picture
-  • Aligning taxation with value creation
- Addressing the “Cash Box”



IFA OECD PANEL

BEPS: THE BIGGER PICTURE

Marlies de Ruiter
Head Tax Treaties, Transfer Pricing &
Financial Transactions Division



1869

Globalisation

2010



Profit

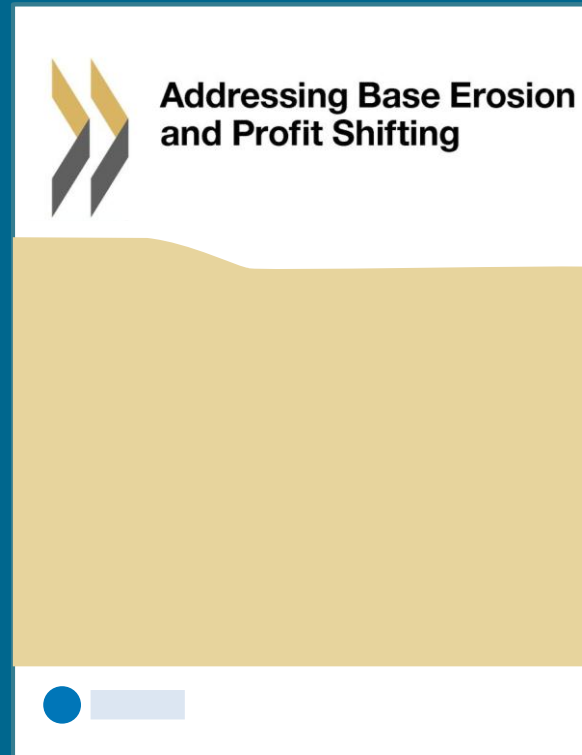
Tax Base



Shifting

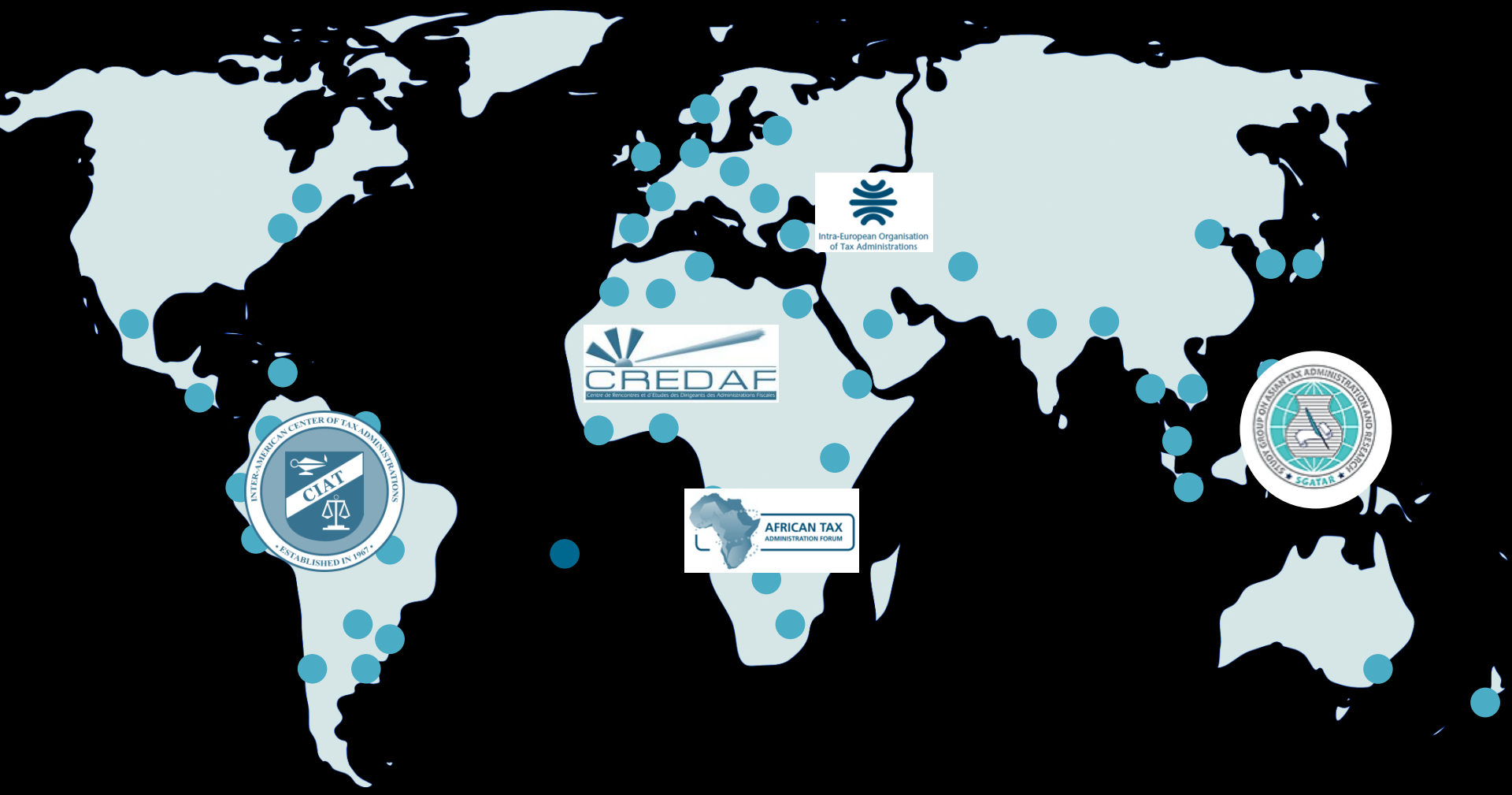


International Tax



February 2013

BEPS Action Plan



International Consensus

Coherence

Hybrid Mismatch Arrangements (2)

Interest Deductions (4)

CFC Rules (3)

Harmful Tax Practices (5)

Substance

Preventing Tax Treaty Abuse (6)

Avoidance of PE Status (7)

TP Aspects of Intangibles (8)

TP/Risk and Capital (9)

TP/High Risk Transactions (10)

Transparency

Methodologies and Data Analysis (11)

Disclosure Rules (12)

TP Documentation (13)

Dispute Resolution (14)

Digital Economy (1)

Multilateral Instrument (15)

Action Items

Question 1

What aspect of BEPS do you expect to have the biggest impact? What changes do you already see occurring?



Question 2

Do you witness a change of the borderline between source and residence taxation due to the BEPS process?



Question 3

Your greatest wish for its finalization and implementation?



ALIGNING TAXATION WITH VALUE CREATION



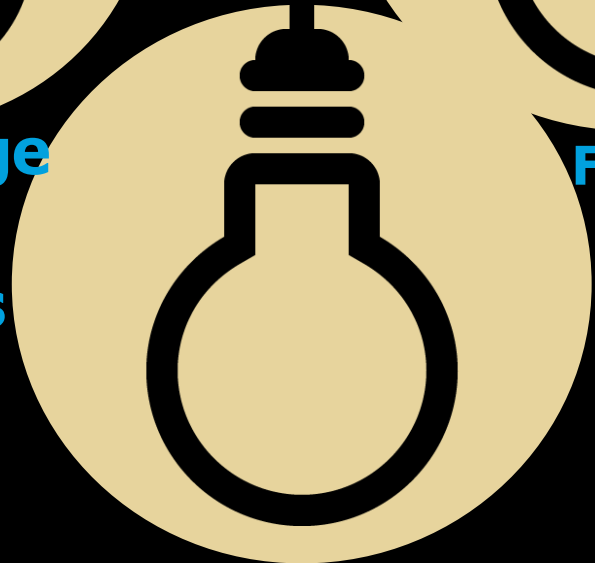
**Exchange
of
rulings**



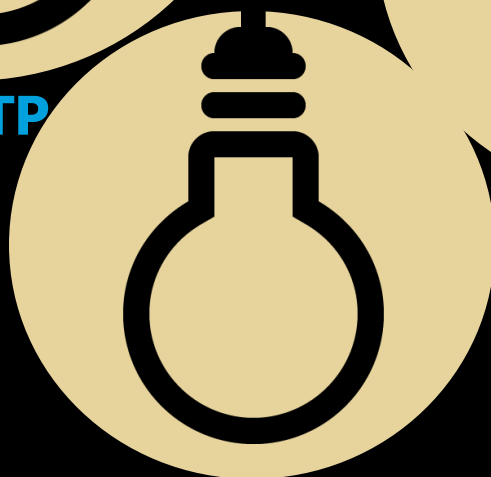
FHTP



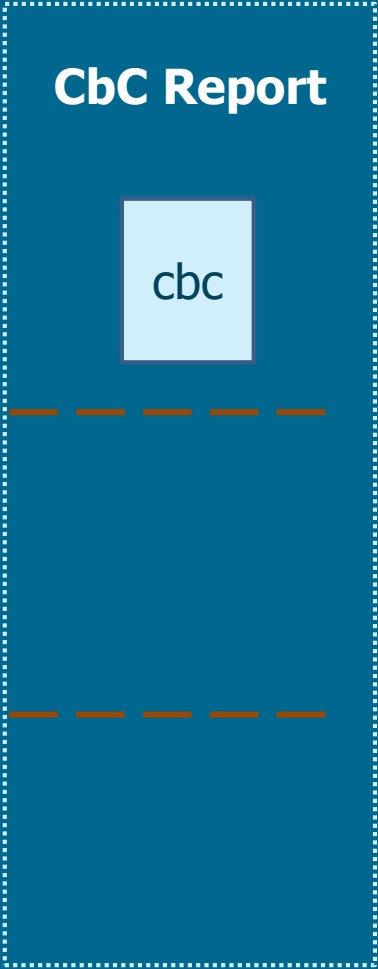
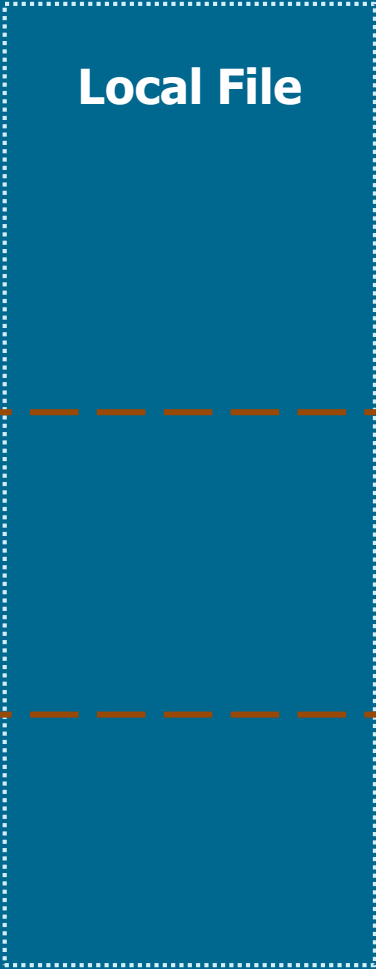
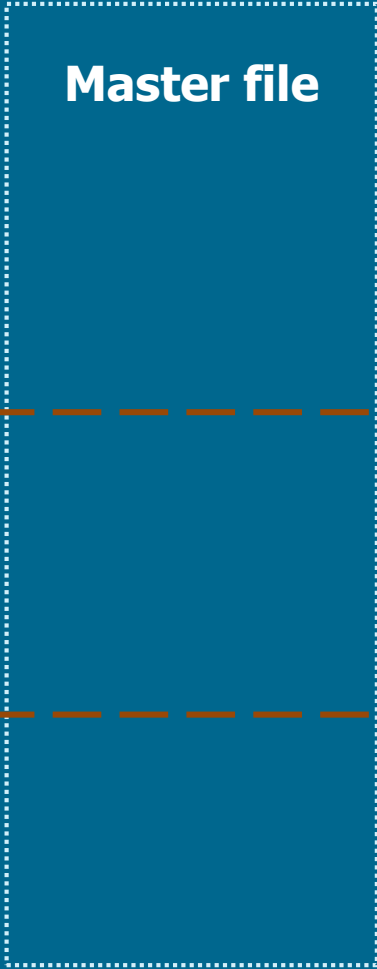
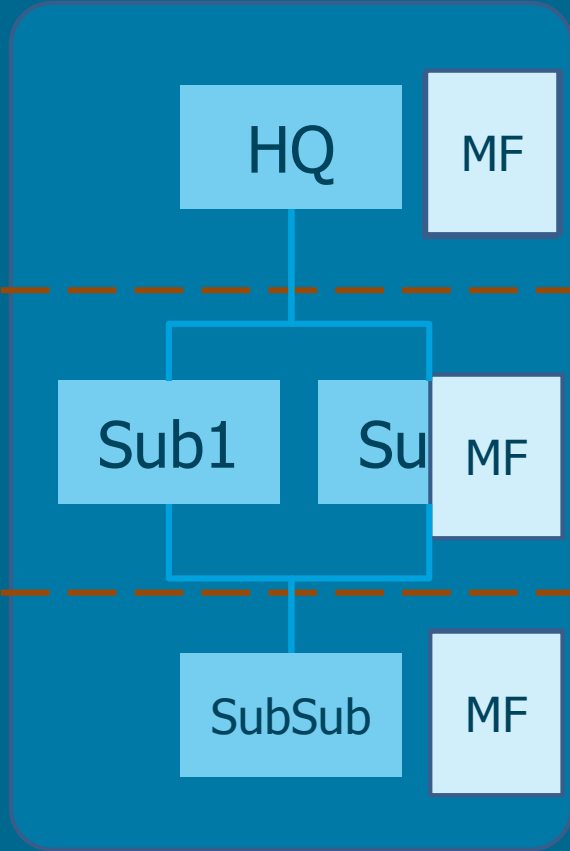
**MAC
Membership**



**Country by
Country
Reporting**



**Mandatory
disclosure**



Large MNE Group

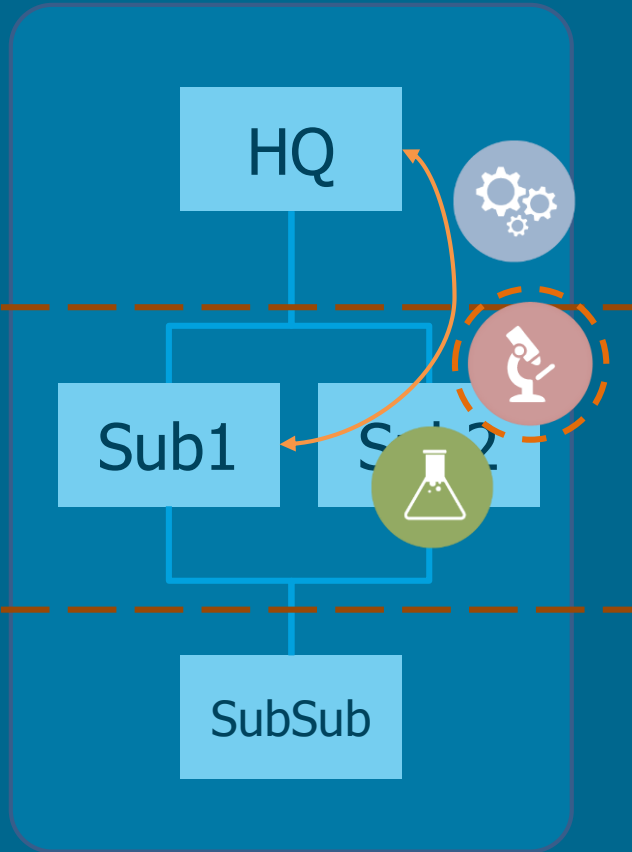
Overview of MNE group business

More detailed information on intercompany transactions affecting local jurisdiction

Aggregate tax jurisdiction wide information

CbC Reporting

I. Careful delineation of the actual transaction between associated enterprises

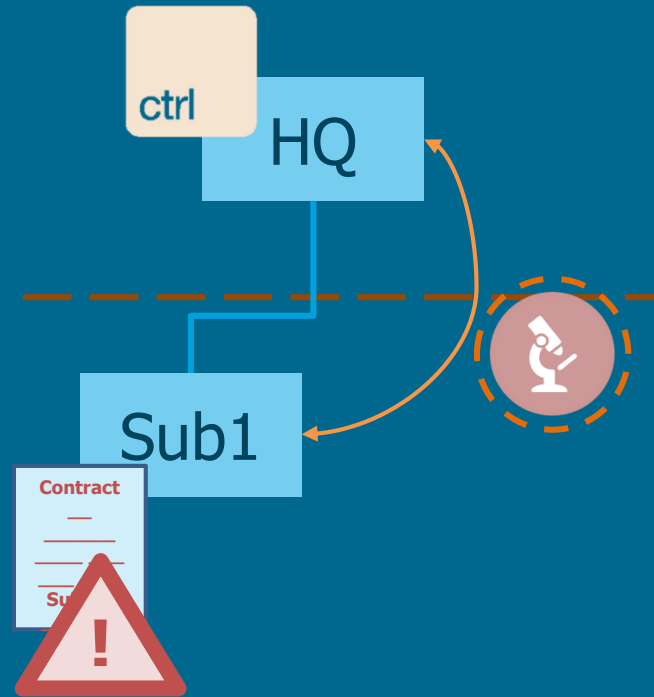


Economically relevant characteristics

1. Contractual terms
2. Functions performed, taking into account assets used and **risks**
- II. **assumed** conditions and the other economically relevant characteristics of the controlled transactions
3. Characteristics of property/service
4. Economic circumstances
5. Business strategies

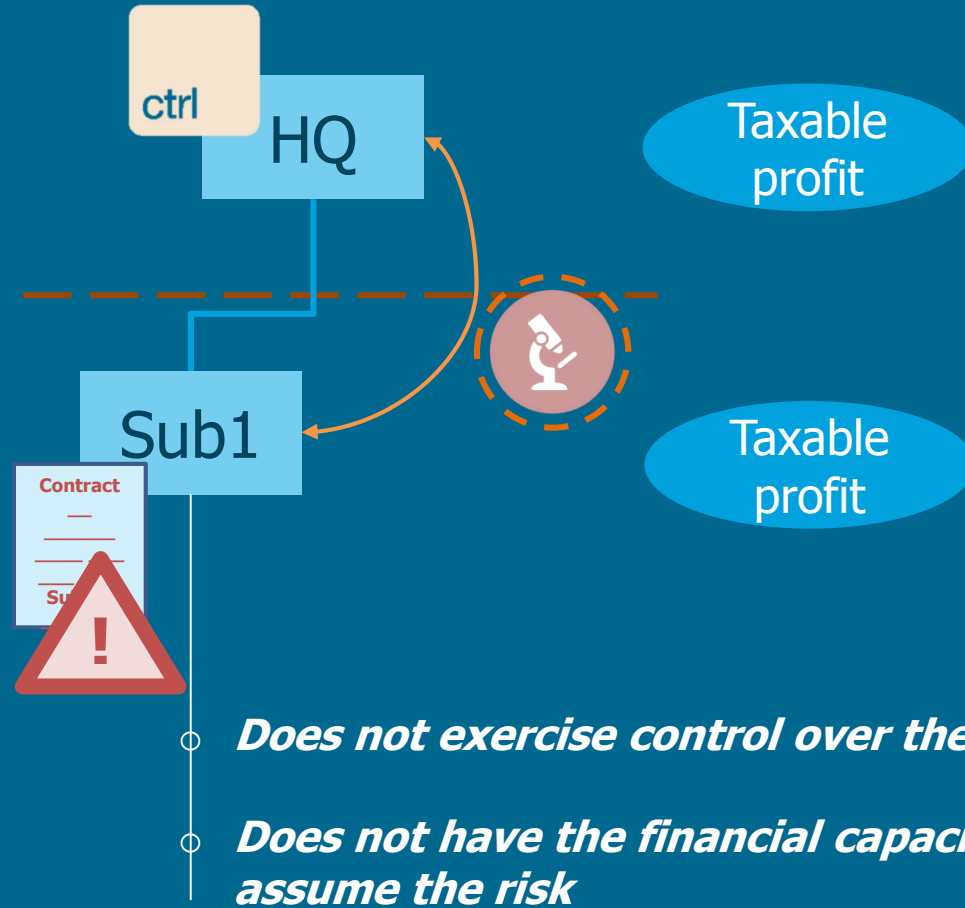
Transfer Pricing

1. Identify risk
2. Determine how risk are contractually assumed
3. Functional analysis
4. Determine whether contractual assumption of risk is consistent with the conduct of the associated enterprises and other facts of the case



Transfer Pricing

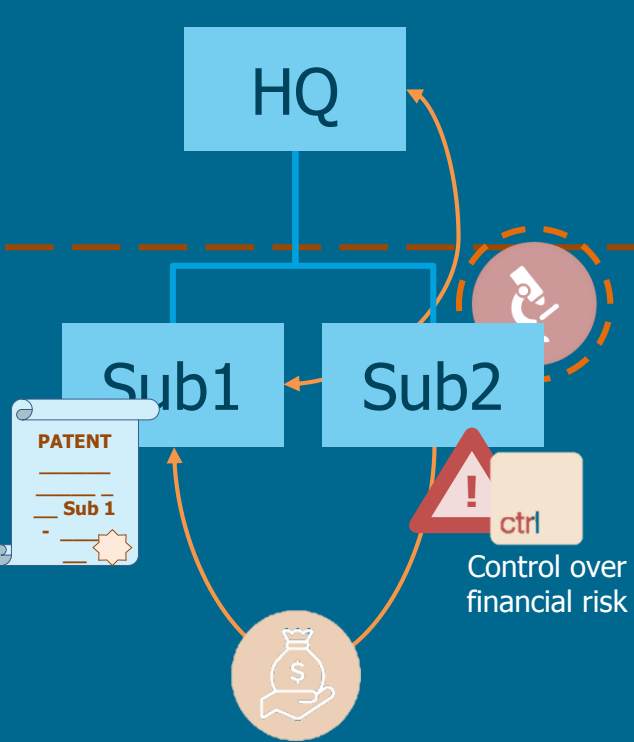
5. Apply guidance for allocation of the risk



Allocation to party that exercises control and has the financial capacity to assume the risk

Guidance on Intangibles

- Follows framework Chapter 1

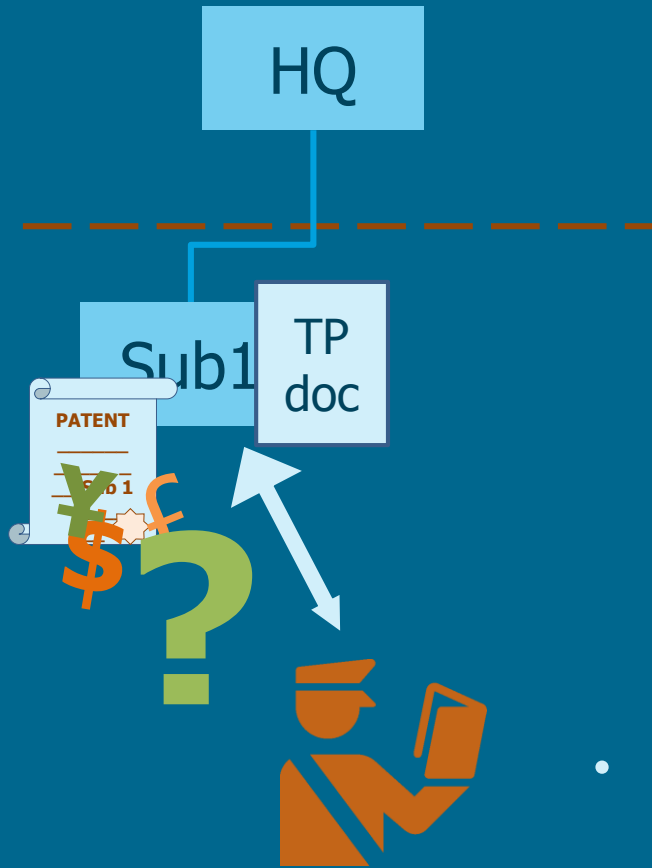


- Funder without performing important functions related to intangible and without assuming the risks related to the intangible:
risk-adjusted financial return if control over financial risk
- Funder without control over financial risk:
no more than risk free financial return

Guidance on Intangibles

Hard-to-Value Intangibles

- Allows taxpayer to demonstrate proper transfer pricing analysis
- Addressing information asymmetries
 - *Ex post* outcomes

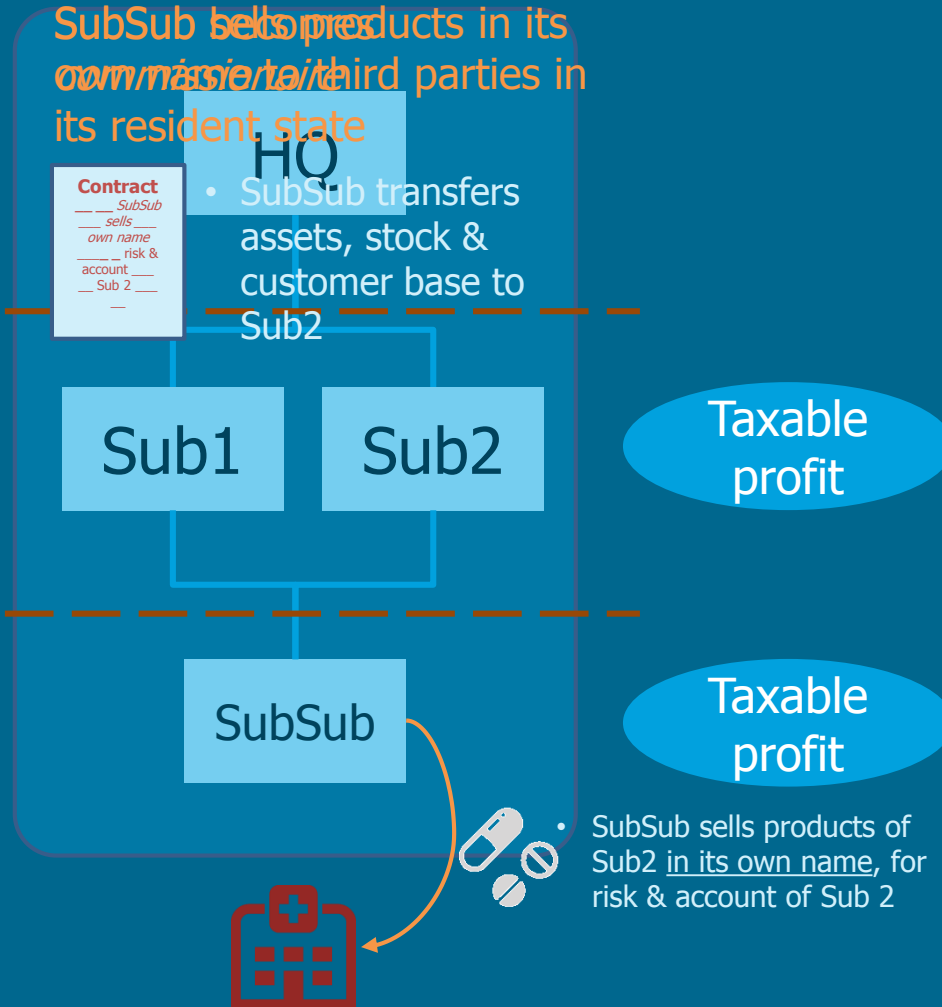


- *Ex ante* pricing agreements

Transfer Pricing

Before:

SubSub sells products in its own name to third parties in its resident state



Taxable profit

Taxable profit

Changes to OECD Model Convention

Article 5(5)

- Departure of formal approach:
- Regular conclusion of contracts to be performed by Sub2 may lead to taxable presence in other Contracting State

Article 5(4)

- Each of exceptions is restricted to activities that are otherwise of a "preparatory or auxiliary" character
- Introduction of anti-fragmentation rule

+ Interaction with PPT

TP Guidelines

Immediately



Tax Treaty Measures

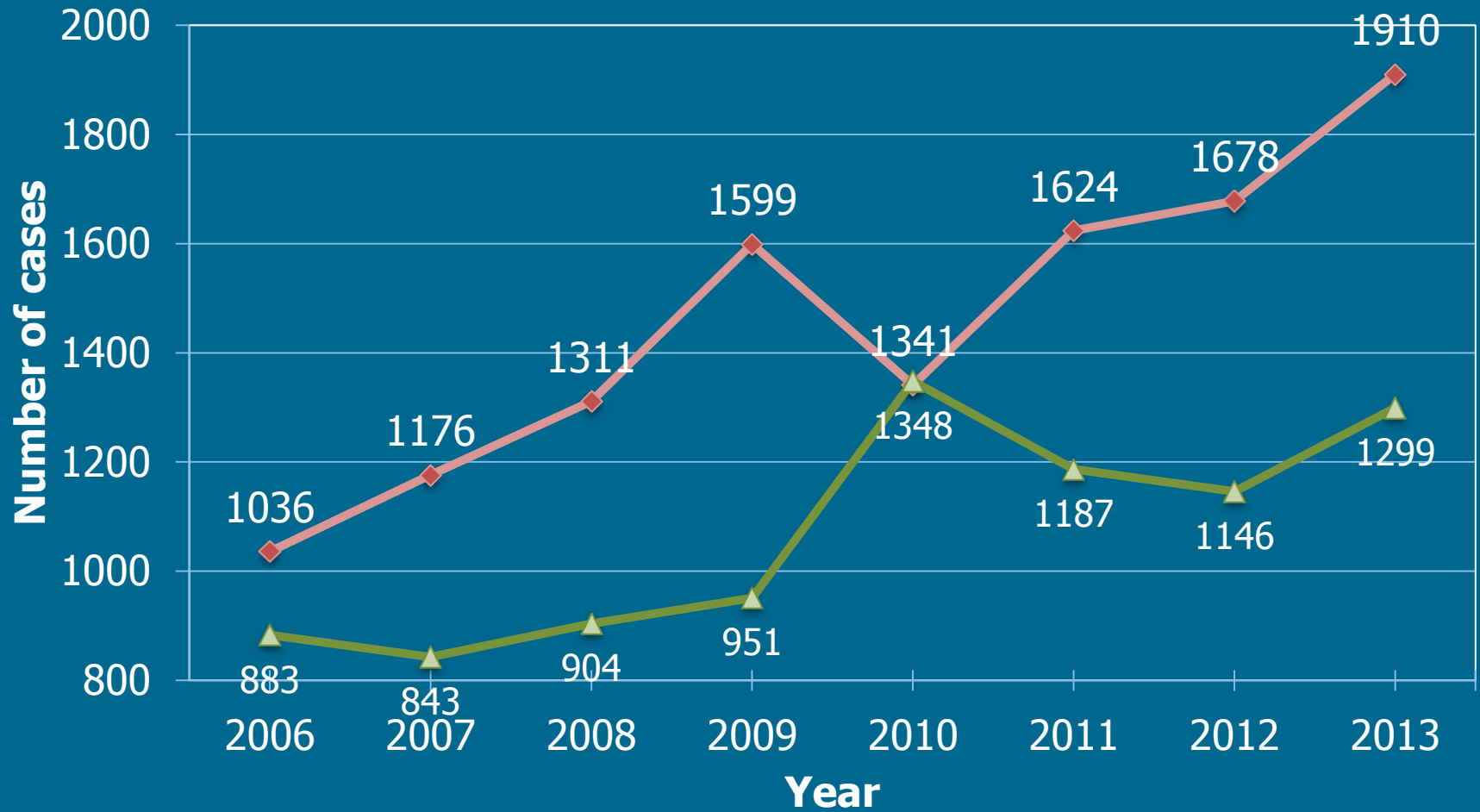
**Renegotiations/
Multilateral instrument**

Domestic Law Measures

Domestic legislative procedures

Implementation

MAP cases **initiated** / **completed** by year



Dispute Resolution



Minimum Standard



Peer review



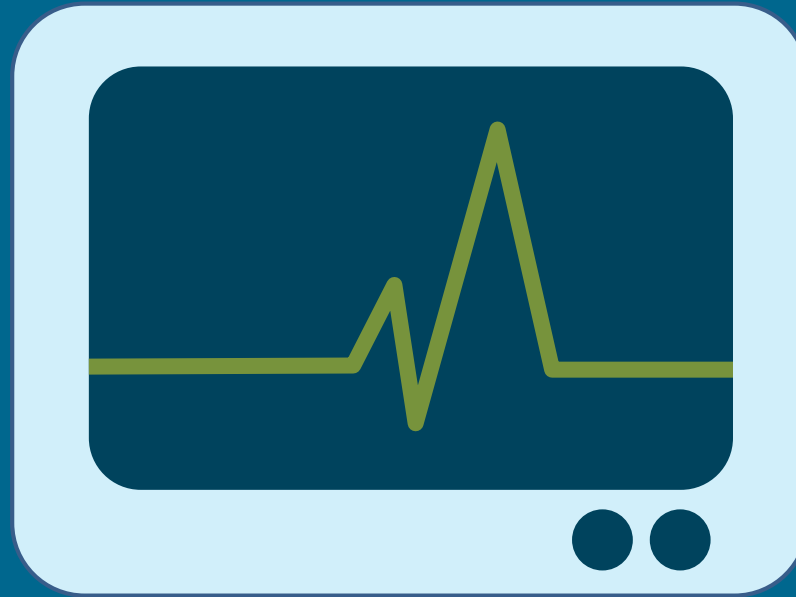
Supplementary commitment

**Mandatory binding
MAP arbitration**

A large group of countries



Dispute Resolution



Monitoring

Transfer Pricing

Financial transactions
Guidance HTVI
Profit Split methods

Interest

Finalise design group ratio
carve-out
Special rules for specific sectors

Treaty Abuse

Treaty entitlement of non-CIVs

Permanent establishments

Clarifying profit attribution

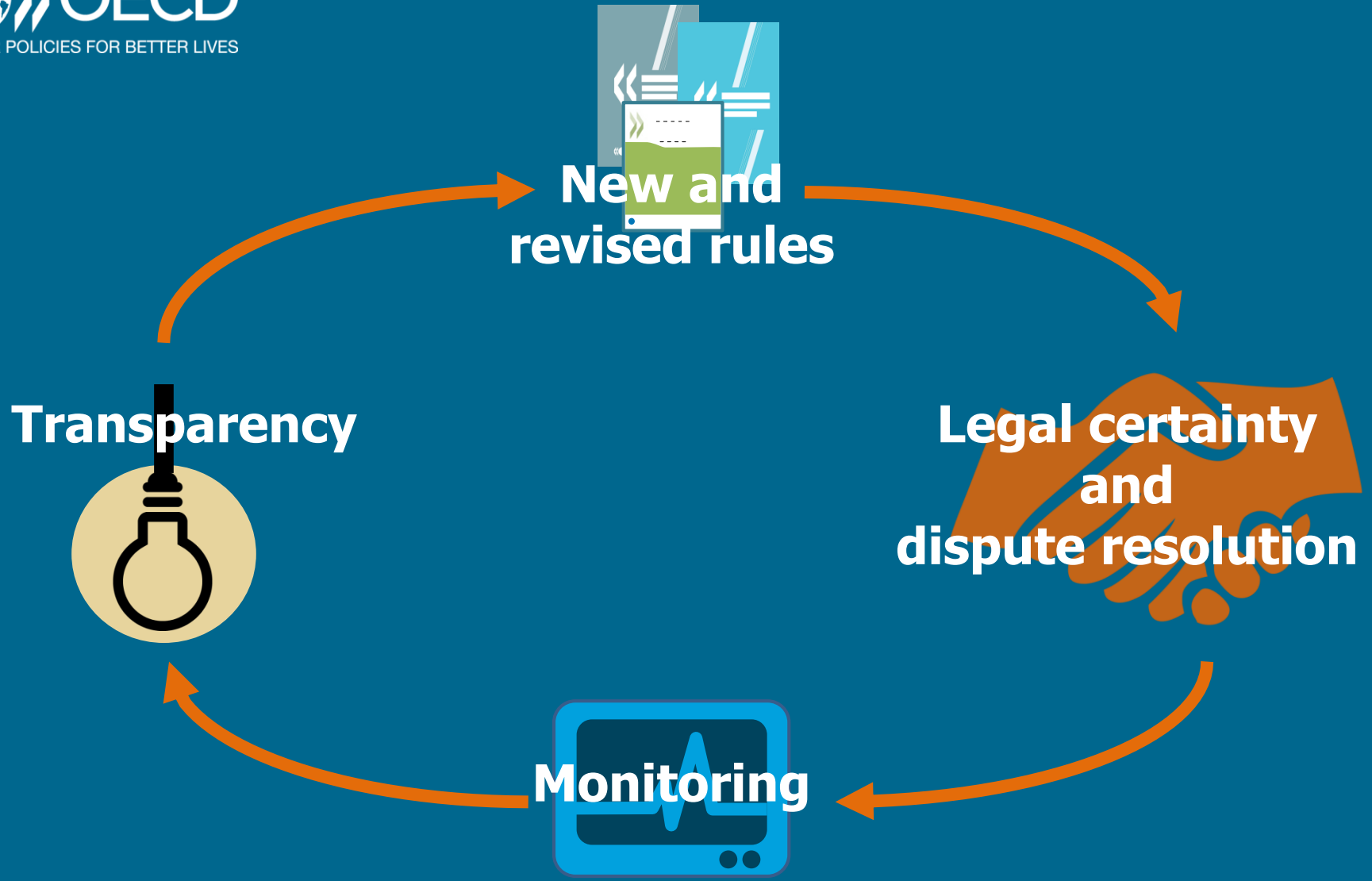
Harmful Tax Practices

Expand participation of non-OECD
members
Revision of HTP criteria

Multilateral instrument

Negotiations by the ad hoc group

Follow-up work



Holistic Approach

Question 4

Is „Aligning taxation with value creation“ an old or a new goal?

To what extent does its implementation require new domestic legislation or the introduction of new treaty provisions?



Question 5

What do we really know about the mismatch between taxation and value creation?

In April 2015, OECD has released a „Discussion Draft“ on BEPS Action 11 named „Improving the analysis of BEPS“. The draft report makes clear that

- existing macroeconomic data do not sufficiently distinguish between real activity and BEPS;
- existing firm level data are currently not framed in order to make that distinction (individual tax returns, financial accounting)

Is this a good starting point?

Question 6

In order to identify useful indicators for „transfer pricing risks and other BEPS related risks“ documentation and „country-by-country reporting“ under Action 13 requires MNEs to submit to tax authorities Master Files, Local Files and CbC Reports.



Are the required data useful (in particular for developing countries) or will they create the background for competing tax claims – and double taxation?


Question 7

Are companies able to comply with CbC rules at proportionate cost?

How are tax authorities going to use these data efficiently? Will they be subject to an information overload? Or do they even need more information?



Under the newly released „implementation package“ MNEs are obliged to file the „CbC Report“ with the tax authorities who are competent for the „ultimate parent“.

 These tax authorities shall exchange the CbC Report annually on an automatic basis with all other tax authorities where „constituent entities“ of the group are resident. This is meant to be negotiated under a „multilateral competent authority agreement“ or by amending existing treaties (either DTCs or TIEAs).

Question 8

How are tax authorities meant to ensure confidentiality? Will there be lists of „unreliable“ countries?

Question 9

 Do we expect widespread consensus on automatic information exchange?

On the basis of this documentation, Actions 8 – 10 are meant to „align taxation with value creation“ in the area of transfer pricing.

Question 10

Under the traditional framework ownership or assets and contractual arrangements played a decisive role? To what extent will the new framework depart from this understanding?

Question 11



What substantial threshold has to be met in order to allocate risk to an entity?

Question 12

Is this (new?) approach in line with existing treaties and domestic legislation?

Additional issues of permanent establishments have been addressed under Action 7 (Preventing the artificial avoidance of PE status). This Action item is not meant to rewrite source rules in a general fashion. It only aims at new business models created by the digital economy and contractual arrangements.

Question 13



Will the „commissionaire arrangements“ become obsolete under Action 7?

Question 14

Will the digital economy be affected by the new rules on „preparatory“ and „auxiliary“ activities?

And now the Coffee Break See you in 30 Minutes!



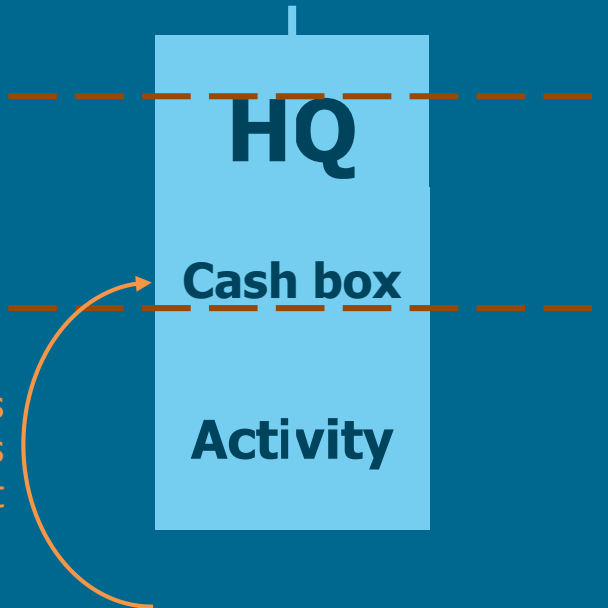
ADDRESSING THE CASH BOX



Crucial element of BEPS structures



Transparency



Action 5
Exchange of ruling

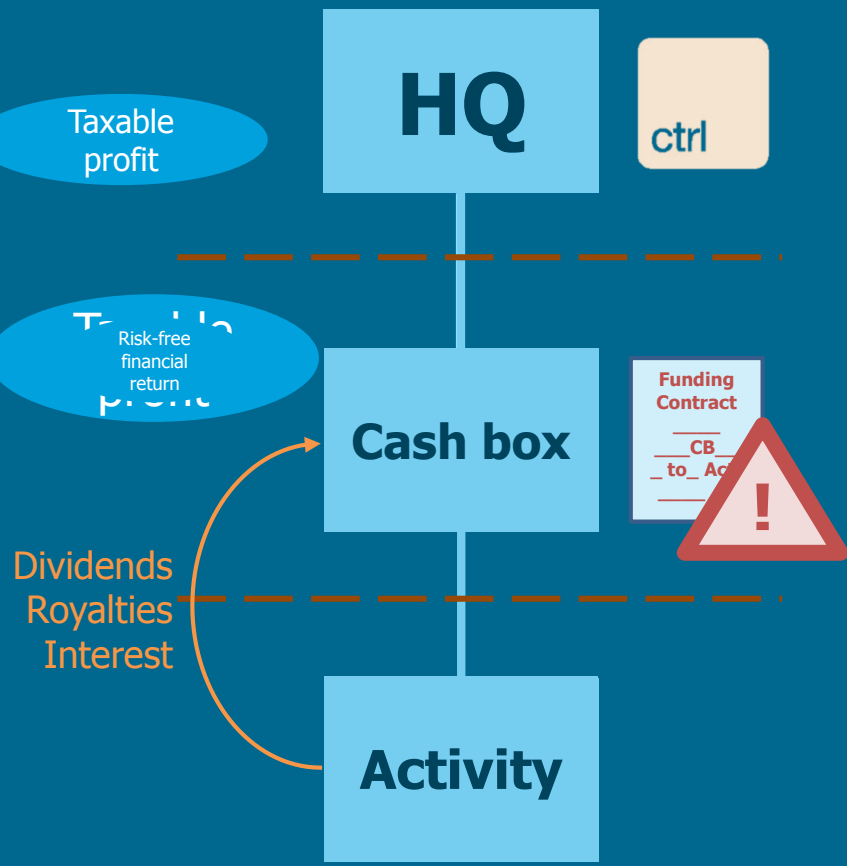
Action 12
Mandatory disclosure

Action 13



*Possibly
deterrent
effect*

Revised transfer pricing guidelines

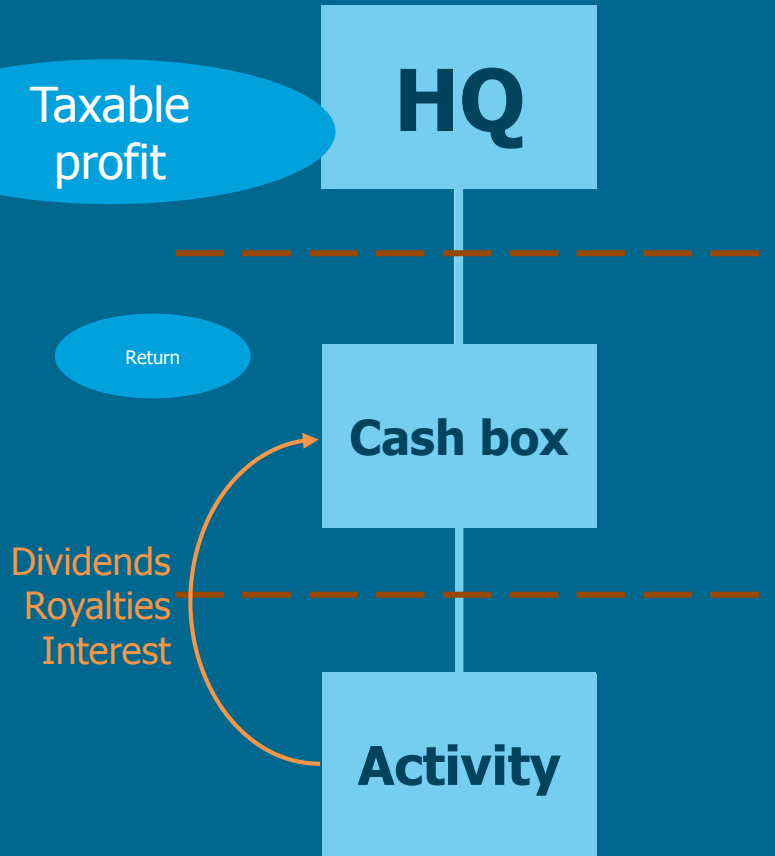


Accurate delineation of the transaction

Does cash box control the risks in relation to the tangible or intangible asset?

Does the cash box control financial risks in relation to the funding?

CFC rules



Alternative building blocks, e.g.

- Thresholds
- CFC Income
 - Categorical analysis*
 - Substantive analysis*
 - Excess profit analysis*

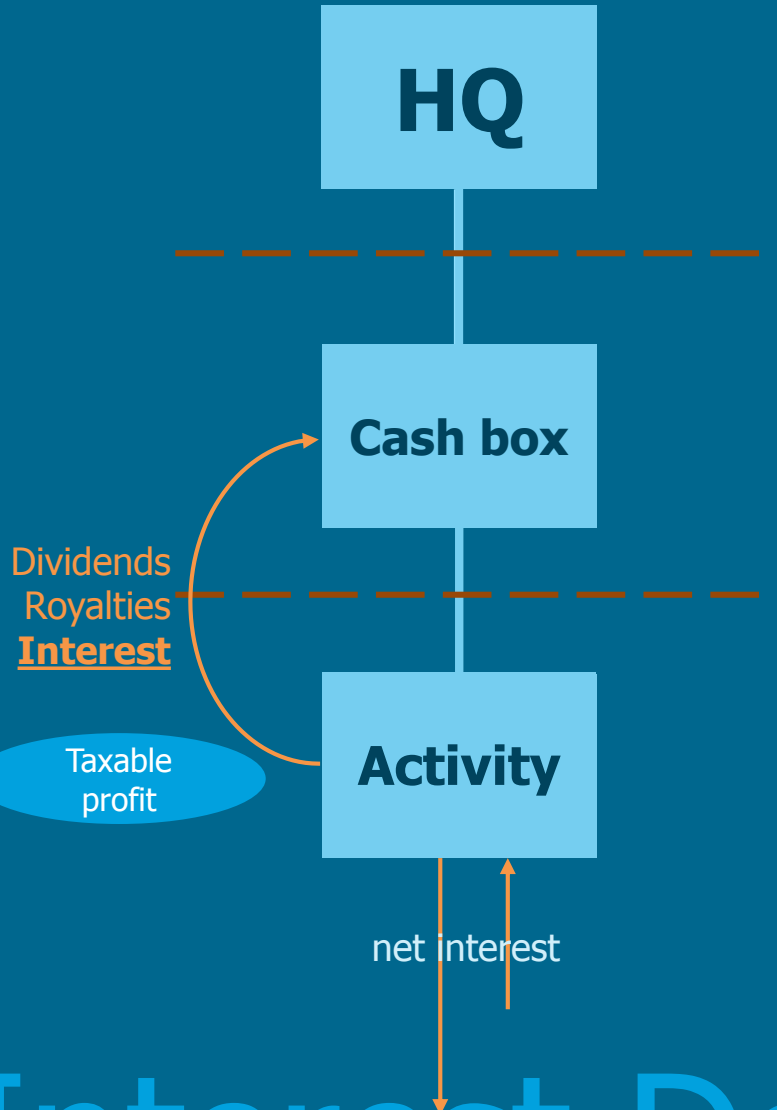
Under (i) and (ii) HQ may be subject to additional tax

Interest deductibility



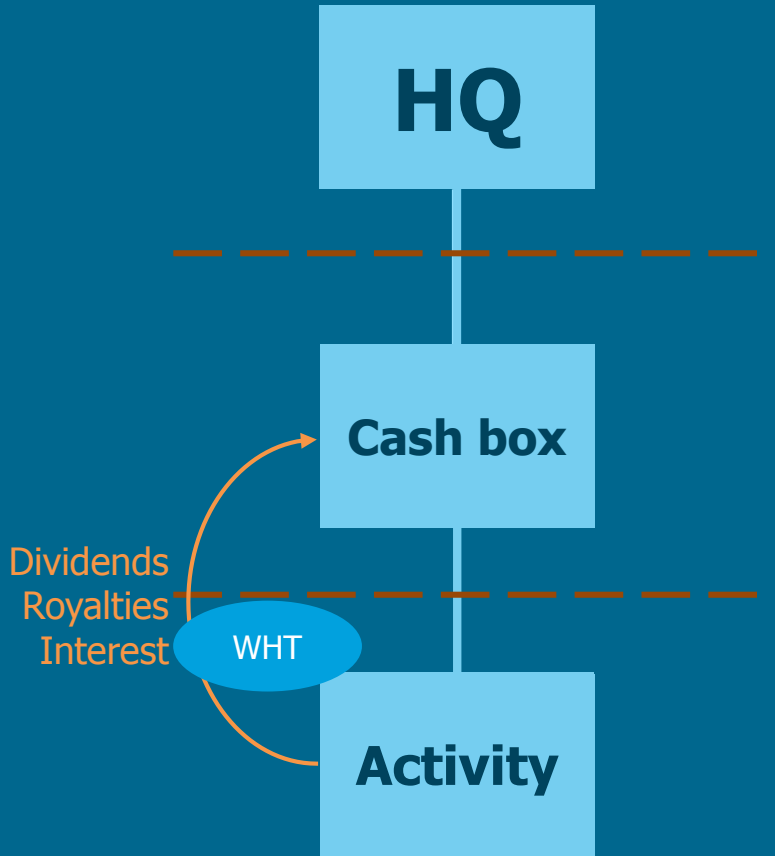
Facilitate the convergence of national rules

- Determine excessive interest: interest over certain interest : income ratio
 - Fixed ratio, or
 - Group ratio



Interest Deductibility

Treaty Abuse

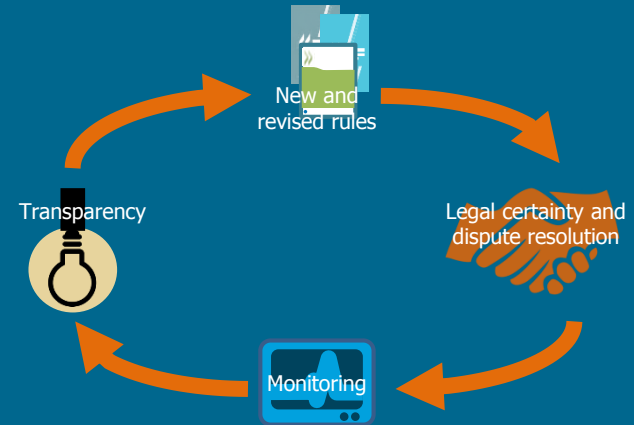
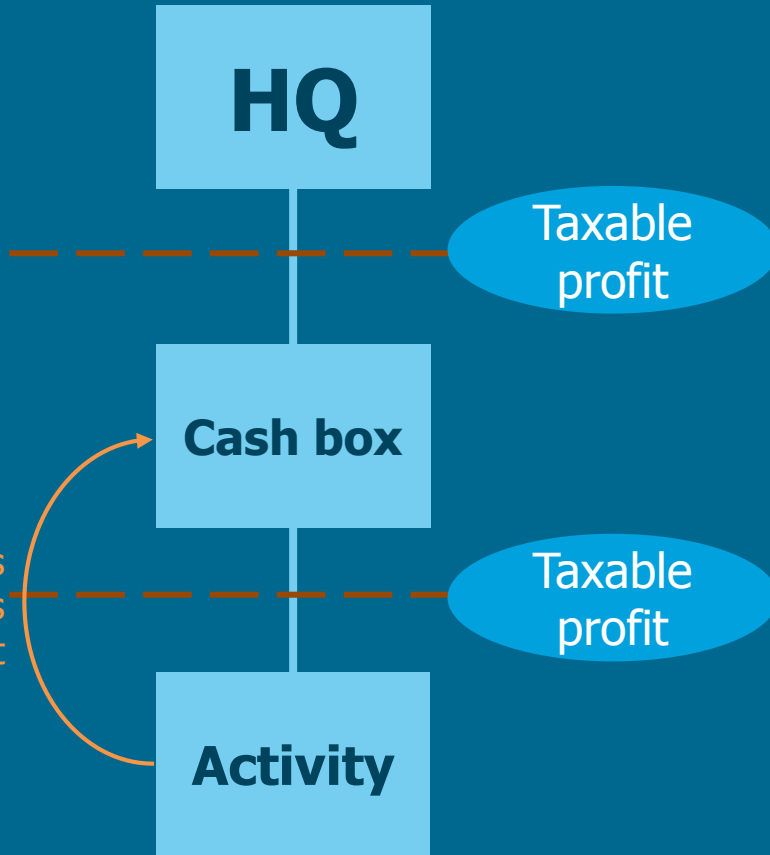


Introduction of a minimum standard preventing treaty abuse

Will Cash box be entitled to treaty benefits?

1. Limitation on Benefits & PPT; or
2. Principal Purpose Test Rule; or
3. LOB supplemented by anti conduit rule

Treaty Abuse



All measures combined

- **Deterrent effect**
- **Alignment taxation and value creation restored**

Overall effect

The „cash box“ is about preventing double non-taxation as the „cash box“ is likely to be established in a low or no tax jurisdiction

The „cash box“ is about aligning taxation with value creation as the „cash box“ is likely not to contribute to the value of the assets.

Under a „holistic view“ the question arises whether taxation should be effected



- in the jurisdiction where intangibles are created
- or in the jurisdiction where the use of intangibles is remunerated

The jurisdiction where the intangible is created has two options to lay their hands on the foreign entity's business profit:

- Application of transfer pricing control to all contractual relations with the „cash box“
- Application of CFC provisions with regard to „cash box“ income



The jurisdiction where the intangible is exploited has the option to

- Levy withholding taxes on outflowing payments
- Limit the deductibility of outflowing payments

Question 15

What are the requirements for profit being allocated to the „cash box“? What decides on the borderline between allocation of the full profit or treatment as a creditor receiving fixed income from funds? Does this work symmetrical if the risk materialises?



Question 16

How shall we value intangibles at the time of transfer? What special measures are to be applied for „hard-to-value“ intangibles? Are these special measures outside or inside the arm's length standard? Do we need amendments to domestic legislation or existing treaties to achieve this goal?

Question 17

What role shall CFC legislation play in the BEPS context? Is it meant as a backstop if no substantial source taxation applies? Or can it take precedence extending the reach of world-wide taxation at the level of the parent company?

Question 18



What is the difference between „traditional“ CFC legislation and new legislation aiming to combat BEPS? Shall CFC legislation apply in the case of foreign-to-foreign stripping?

Question 19

To what extent will new LOB-provisions or „principal purpose tests“ (Action 6) change the landscape of withholding taxation on royalties and interest payments?



Question 20

Under Action 4, the existing Discussion Draft only lays out different options to limit deductibility of interest (group-wide limits or entity-related limits; reference to assets, earnings (including EBITDA) or debt/equity ratios; targeted or general measures).

Is there any „best practice“ emerging?



Question 21

It is said that we need more international coordination in this area – in order to avoid over- (double) or under-taxation of interest payments. Is this on the horizon? Action 4 is skeptical on „linking“ non-deduction of interest with re-characterisation in the recipient’s jurisdiction.

Procedural Back-Up – Granting transparency and certainty to tax authorities and to taxpayers

Question 22

Action 12 pleads for a coordinated effort to require „mandatory disclosure“ of tax avoidance schemes. A number of countries has already introduced similar disclosure rules. What role shall disclosure of tax shelters play internationally?

Implementation of the BEPS results under domestic and international law will lead to a major upheaval in international tax treatment. There is growing fear that BEPS concepts („aligning taxation with value creation“) and increased transparency (e.g. „country-by-country-reporting“ and disclosure of tax avoidance schemes) will lead to a surge in overlapping tax claims and double taxation.

Action 14 looks for adequate instruments of dispute resolution. The Draft is skeptical about consensus for arbitration and pleads for political commitments to improve MAP and APA procedures.

Question 23

To what extent shall future dispute resolution go beyond existing treaty practice? Are current proposals sufficient in that respect?

BEPS Impact and BEPS Implementation

Question 24

The Ad Hoc Group on the multilateral instrument is set to start substantive work in October 2015. What is the perspective for the „multilateral instrument“? Is it necessary? And is it an „option realistically available“?



Question 25

The United States have declared not to participate in the multilateral instrument. What is the option for future U.S. tax policy? Which items of the BEPS project will play a major role in that context?

Question 26

Is BEPS useful for developing countries?



Question 27

Will the business community be overwhelmed by additional compliance burdens?

Question 28

 Will tax authorities be overwhelmed by additional administrative burdens?

Question 29

Looking back to the last two years, has BEPS moved the international tax system towards greater coherence?

