G8/G20 TAXATION ISSUES :

Tax Training Day, ODI, London
16 September 2013

OECD
BETTER POLICIES FOR BETTER LIVES

BASE EROSION AND PROFIT SHIFTING

OECD Work on Taxation

- Focus has historically been on the development of common standards to eliminate double taxation for cross border investments
  - Model Tax Convention, which serves as the basis for over 3,000 bilateral tax treaties
  - Transfer Pricing Guidelines, which provide common standards for allocating income among members of a multinational group
- Prevention of double taxation remains core work but there is now recognition that the issue of double non-taxation due to base erosion and profit shifting (BEPS) should also be tackled

Increased Attention on BEPS

- Increased attention of mainstream media on corporate tax affairs
- Spreading perception that MNEs dodge taxes all around the world, in particular in developing countries
- Debate on BEPS issues has reached a high political level
  - G20 Leaders in Los Cabos, 19 June 2012
  - G20 Finance Ministers in Mexico City, 5 November 2012
  - BRICS joint communiqué, 18 January2013

Increased Attention on BEPS

- **G20 Finance Ministers Meeting, 18-19 April 2013, Washington**

"We welcome the progress made in the development of an action plan on tax base erosion and profit shifting by the OECD and look forward to a comprehensive proposal and a substantial discussion at our next meeting in July."

- **G8 Lough Erne Declaration, 18 June 2013**

"1. Tax authorities across the world should automatically share information to fight the scourge of tax evasion.

2. Countries should change rules that let companies shift their profits across borders to avoid taxes, and multinationals should report to tax authorities what tax they pay where.

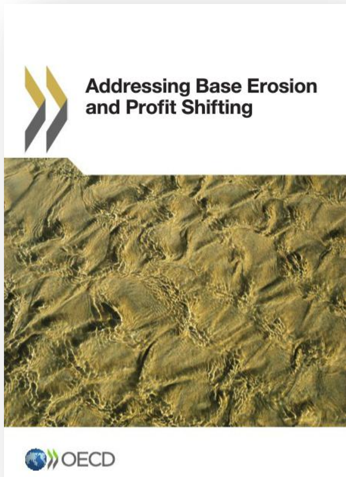
3. Companies should know who really owns them and tax collectors and law enforcers should be able to obtain this information easily.

4. Developing countries should have the information and capacity to collect the taxes owed them – and other countries have a duty to help them. (…)"

- **G20 Leaders Declaration, 6 September 2013**

We fully endorse the ambitious and comprehensive Action Plan – originated in the OECD – aimed at addressing base erosion and profit shifting with mechanism to enrich the Plan as appropriate. We welcome the establishment of the G20/OECD BEPS project and we encourage all interested countries to participate.

Report: Addressing BEPS



- *Addressing Base Erosion and Profit Shifting* published on 12 February 2013
  - ➢ Identifies main pressure areas leading to opportunities for BEPS
  - ➢ Calls on governments to address these areas: in a nutshell, if governments are not happy with the results under the laws, they must change the laws
- Sent to and discussed at G20 Finance Ministers meeting in Moscow on 15-16 February 2013:

  "[W]e welcome the OECD report on addressing base erosion and profit shifting and acknowledge that an important part of fiscal sustainability is securing our revenue bases. We are determined to develop measures to address base erosion and profit shifting, take necessary collective actions and look forward to the comprehensive action plan the OECD will present to us in July"

  - G8 Leaders Meeting, 13-14 June 2013, Lough Erne

Key Tax Principles and Opportunities for BEPS

- In practice, any structure aimed at BEPS incorporates a number of co-ordinated strategies, which often can be broken down into four elements
  - Minimisation of taxation in a foreign operating or source country either by shifting gross profits via trading structures or reducing net profit by maximising deductions at the level of the payer
  - Low or no withholding tax at source
  - Low or no taxation at the level of the recipient (via low-tax jurisdictions, preferential regimes, hybrid mismatch arrangements) with entitlement to substantial non-routine profits via intra-group arrangements
  - No current taxation of the low taxed profits at level of ultimate parent. Further, effective cash repatriation strategies and "permanent" foreign reinvestment of low taxed cash
- The Report identifies a number of pressure areas e.g. hybrids, preferential regimes, anti-avoidance rules, etc.

Developing the Action Plan on BEPS

- Following the February report, all OECD Members and several non member countries in the Committee on Fiscal Affairs participated in the work to develop the Action Plan, including Argentina, China, India, Russia, and South Africa.
- The development of the Action Plan was also informed by engagement with business and civil society (consultations with BIAC, TUAC and NGOs)
- The Action Plan was approved at the meeting of the Committee on Fiscal Affairs on 25 June 2013. All G20 countries participated. It was published on 19 July 2013

The BEPS Action Plan

- The action plan calls for 15 actions organised around the following *three* main pillars:
  - The ***coherence*** of corporate tax at the international level
  - A realignment of taxation and ***substance***
  - ***Transparency***, coupled with certainty and predictability
- It also calls for targeted work in the area of the **digital economy**, which cuts across all three of the main pillars but also presents a number of specific features
- The action plan also calls for the development of a **multilateral instrument** to implement the measures developed under the action plan
- G20 Finance Ministers Meeting, 18-19 July 2013, Moscow
- G20 Leaders Meeting, 5-6 September 2013, St. Petersburg

The Digital Economy (Action 1)

- Spread of the digital economy poses challenges for international taxation
- The digital economy is characterised by an unparalleled reliance on intangible assets, the massive use of data (notably personal data), the widespread adoption of multi-sided business models capturing value from externalities generated by free products, and the difficulty of determining the jurisdiction in which value creation occurs
- Fundamental questions exist as to how enterprises in the digital economy add value and make their profits, and how the digital economy relates to the concepts of source and character of income for tax purposes

Coherence (Actions 2 through 5)

The Action Plan calls for the development of international standards to ensure the coherence of corporate tax at the international level:

• This relates to the need to complement existing rules to prevent double taxation with instruments that prevent double non-taxation.

➢ Neutralise the effects of hybrid mismatch arrangements (action 2)

➢ Strengthen controlled foreign companies (CFC) rules (action 3)

➢ Limit base erosion via interest deductions and other financial payments (action 4)

➢ Counter harmful tax practices more effectively (action 5)

Substance (Actions 6 through 10)

The Action Plan calls for a realignment of taxation and substance:

•This is about treaty abuse and transfer pricing, where the current rules do not always produce appropriate results

➢Prevent treaty abuse (action 6)

➢Prevent the artificial avoidance of PE status (action 7)

➢Assure that TP outcomes are in line with value creation (actions 8, 9, 10)

Transparency and Certainty

BEPS requires greater transparency and certainty:

- Establish methodologies to collect and analyse data on BEPS and the actions to address it (action 11)
- Require taxpayers to disclose their aggressive tax planning arrangements (action 12)
- Re-examine transfer pricing documentation (action 13)
- Make dispute resolution mechanisms more effective (action 14)

Developing a Multilateral Instrument (Action 15)

- Some actions will result in changes to the OECD Model Tax Convention and changes to the OECD Model Tax Convention are not directly effective without amendments to bilateral tax treaties
- If undertaken on a purely treaty-by-treaty basis, the sheer number of treaties in effect will make such a process very lengthy
- There is a need to consider innovative ways to implement the measures resulting from the work on the BEPS Action Plan

An Inclusive Project

- OECD/G20 BEPS Project launched: non-OECD G20 countries on an equal footing with OECD Members
- Developing countries involved through several mechanisms
- Business and civil society representatives will be invited to comment on the different proposals developed in the course of the work

TAX INSPECTORS WITHOUT BORDERS INITIATIVE

TIWB: Background

- In mid-2012, the OECD’s Task Force on Tax and Development began a one year feasibility study to explore the *Tax Inspectors Without Borders* proposal
- The feasibility study considered:
  - The nature of demand for hands-on tax audit assistance
  - The feasibility of providing such assistance

TIWB

- The TIWB objective is to enable the transfer of tax audit knowledge and skills to tax administrations in developing countries
- This will be through a real time, “learning by doing” approach

TIWB

Aims of TIWB expert deployments

- Experts will be deployed to work directly with local tax officials on current audits and audit-related issues concerning international tax matters, and to share general audit practices.

•In addition to improvements in the quality and consistency of audits and the transfer of knowledge to recipient administrations (tax administrations seeking assistance), broader benefits are also anticipated.

TIWB

<u>Aims of TIWB expert deployments</u>

- These include:
  - The potential for more revenues,
  - Greater certainty for taxpayers and;
  - Encouraging a culture of compliance through more effective enforcement

TIWB

- A final report on the feasibility study was considered and approved by the OECD's CFA and DAC in late June 2013.
- **G8 Lough Erne Declaration, 18 June 2013**

"We welcome the OECD's feasibility study for its Tax Inspectors Without Borders proposal to assist tax administrations investigate specific and complex tax cases. We will take practical steps to support this initiative, including by making tax experts available."

- **G20 Leaders Declaration, 6 September 2013**

"We welcome the OECD Tax Inspectors without Borders initiative, which aims to share knowledge and increase domestic capacities in developing countries in the tax area."

TIWB

- The final report on the feasibility study into TIWB can be found on the OECD website
- The OECD aim to launch TIWB in early 2014, after a 6 month implementation period that includes a number of pilot expert deployment projects
- TIWB will be developed initially as a project of the Tax and Development Programme of the OECD

TIWB

TIWB Secretariat

- A small TIWB Secretariat will be established within the OECD's Tax and Development Programme.
- Its role is to facilitate the deployment of experts who will provide real-time tax audit assistance to developing countries.
- The TIWB Secretariat can be contacted at caroline.malcolm@oecd.org.
- New developments can be followed on the Twitter account @ Tax_Inspectors

TAX AND DEVELOPMENT TASK FORCE PROGRAMME

Tax and Development Task Force and Programme

- Four year (2011-2014) Tax and Development Programme and Task Force.
  - Joint initiative of OECD's Committee for Fiscal Affairs (CFA) and Development Assistance Committee (DAC)
  - Horizontal project integral to the OECD's Development Strategy

- Objective is to create an enhanced enabling environment to assist developing countries collect taxes effectively and fairly

- Flexible membership drawn from OECD countries; developing countries; international/regional organisations; business; civil society
  - Advisory role to OECD Committees

- Co-chaired by Netherlands and South Africa

Taxation of Multinational Enterprises: Transfer Pricing

Objective: To increase the capacity of developing countries to adopt, and effectively implement, transfer pricing rules in accordance with internationally agreed principles

Operates through a partnership with the EU and WB/IFC. Capacity development initiatives in Colombia, Ghana, Kenya, Rwanda and Vietnam

- Integrated with existing country tax reform initiatives – working with donor agencies on the ground (e.g., GIZ in Ghana)
- Provides assistance to regional organisations (e.g. ATAF, EAC) and develops new guidance and tools
- Tests the applicability and relevance of OECD guidance on transfer pricing to the developing country context

Transfer Pricing: Impacts

Colombia: An increase of over 70% in the revenue collected from transfer pricing adjustments (from USD 3.3M in 2011 to USD 5.83M in 2012); new transfer pricing legislation passed, organizational restructuring and risk assessment procedures in place

Ghana: New transfer pricing regulations passed into law, administrative redesign and a new Transfer Pricing Practice Note for the guidance of taxpayers and tax officers agreed

Kenya: An increase in the number of audit cases completed, revenue collected, and number of cases going to dispute resolution. In a recent case KRA negotiated a transfer pricing adjustment resulting in additional tax revenue of USD 12.9M. In a second case the Kenyan Judiciary ruled in favour of the KRA resulting in additional revenue of USD 10.9m

Rwanda: A full assessment of the risk of profit shifting, as the basis on which a new transfer pricing regime is being planned

Vietnam: A significant increase in the tax administration's capacity to enforce its transfer pricing rules. A recent audit of a large MNE resulted in increased tax paid of USD 3.9M

AUTOMATIC EXCHANGE AND DEVELOPMENT OF A STANDARDISED MODEL

Automatic Exchange - the Global Standard

- **G20 Leaders Declaration, 6 September 2013, Saint Petersburg**

*"We commend the progress recently achieved in the area of tax transparency and we fully endorse the OECD proposal for **a truly global model** for multilateral and bilateral automatic exchange of information."*

- **Timescale for the Global Standard**

*"Calling on all other jurisdictions to join us by the earliest possible date, we are committed to automatic exchange of information as **the new global standard**, which must ensure confidentiality and the proper use of information exchanged, and we fully support the OECD work with G20 countries aimed at presenting such a new single global standard for automatic exchange of information by February 2014 and to finalizing technical modalities of effective automatic exchange by mid-2014."*

Building Capacity for Automatic Exchange

- **G20 Leaders Declaration, 6 September 2013, Saint Petersburg**

"Developing countries should be able to reap the benefits of a more transparent international tax system, and to enhance their revenue capacity, as mobilizing domestic resources is critical to financing development. We recognize the importance of all countries benefitting from greater tax information exchange."

"We are committed to make automatic exchange of information attainable by all countries, including LICs, and will seek to provide capacity building support to them."

"We call on the Development Working Group in conjunction with the Finance Track, to work with the OECD, the Global Forum and other IOs to develop a roadmap showing how developing countries can overcome obstacles to participation in the emerging new standard in automatic exchange of information, and to assist them in meeting the standard in accordance with the action envisaged in the St Petersburg Development Outlook."

G8 Lough Erne – Progress in June 2013

- *The OECD presented*

  'A Step Change in Tax Transparency'

  http://www.oecd.org/ctp/exchange-of-tax-information/taxtransparency_G8report.pdf

- *G8 endorsed the approach in that report*:
- *"We see recent developments in tax transparency as setting a new standard and commit to developing a single truly global model for multilateral and bilateral automatic tax information exchange building on existing systems. We support the OECD report on the practicalities of implementation of multilateral automatic exchange and will work together with the OECD and in the G20 to implement its recommendations urgently."*

Work on Automatic Exchange – Three Steps

- Common agreement on the scope of reporting and exchange including related due diligence procedures
  - A draft has already been discussed by governments and business and further work is on-going
- Legal basis and confidentiality
  - The Multilateral Convention has 56 signatories
  - Article 26 Model Tax Treaty & other legal instruments
- Technical and IT aspects
  - Being developed based on earlier work

How Will We Achieve a Standardised Multilateral Automatic Exchange Model?

- With the full the support of the G8 and the G20 and in close cooperation with the EU, the OECD, working with G20 countries, is now making very good progress in developing a global model of automatic exchange of information expected to be completed in 2014
- Further meetings in October 2013 - with involvement of the Business & Industry Advisory Committee to the OECD as well as government and EU representatives, will work further on a Common Standard of Reporting and Due Diligence
- Global standard proposals February 2014 and final agreement June 2014