BEPS fireworks

International Tax

01 October 2015

Bill Dodwell looks forward to 5 November when formal negotiations begin on the BEPS project

By the time this article appears, the 13 papers covering the 15 actions in the Base Erosion and Profit Shifting (BEPS) project will have been released. The most important questions are whether they will lead to change and when that might happen.

Many states agree that country-by-country tax reporting to tax authorities should be introduced. The line-up of nations producing draft legislation on this includes Australia, China, Mexico, Poland, Spain and the UK. Country-by-country reporting (CbCR) is the only action for which there is a fixed global template for its introduction, such that countries will implement it identically. The reference period starts from 1 January 2016 and the first data must be delivered electronically by 31 December 2017. OECD Secretary-General Angel Gurria recently told the G20: ‘On 5 November, we will hold a signing ceremony of the multilateral Competent Authority Agreement that will enable the automatic exchange of CbCR information by all interested countries.’ This opens up the benefit of enhanced information to a wide range of nations, answering the NGOs, which have lobbied hard for developing countries to gain access to company information. However, access to data will depend on having systems to receive it and agreeing on its confidentiality – a concern of business and many governments.

The next big area likely to see imminent change is transfer pricing. Three actions will lead to substantial revision of the guidelines used by most OECD members and by many other countries as the main guide to methodology. The new version will not emerge until 2017. A few countries – including the UK – include the guidelines in their domestic law, which presumably must mean that their changes cannot take effect until the new ones are published. Most countries, though, use the guidelines as treaty interpretation and it is thus likely we shall see some tax authorities start to use the new chapters immediately. This will be a concern because we could find new guidance being applied to the past when tax years are open. Implementing the new guidelines without the dispute resolution mechanisms set out in action 14 entering into effect is also problematic.

There is a programme of work planned for 2016 because it has not been possible to complete all the actions. Pascal Saint-Amans, director of the OECD Centre for Tax Policy and Administration, told the International Fiscal Association’s (IFA) congress in Basel that there would be work in several areas:

- Interest – more work on the group ratio fall-back and on specific rules for special sectors.
- Permanent establishment – guidance on profit attribution.
- Treaty abuse – guidance on the approach to funds that are not widely held such as private equity funds and real estate funds.
- Transfer pricing – more work on hard-to-value intangible assets, financial transactions and when profit split methods should be used.

The formal negotiations on the multilateral convention, involving more than 80 countries, start on 5 November, and are expected to finish by the end of 2016. Jurisdictions such as the Channel Islands and the Isle of Man have indicated they will seek observer status. The open issue is that the US has not declared that it will join. The multilateral convention is the best way to introduce the significant permanent establishment, treaty abuse and dispute resolution changes, although no doubt the new provisions will also make their way into bilateral negotiations.

Dispute resolution is an important action since the changes are likely to lead to many more disputes between taxpayers and tax authorities, and then between countries. The action will commit countries to better access and process and to invest more in the staff that operate mutual agreement procedures. It is also clear that more than 20 countries are prepared to adopt binding arbitration – on a ‘last best offer’ basis, where the arbitrator selects one of the two offers made by the respective countries. This would be best implemented by the multilateral convention but this would require that the US participate since it is a leading supporter of arbitration in tax treaties (as is the UK).

What about the actions that require domestic law changes? The most important is interest restrictions. It is clear from the public consultation that there was disagreement between the countries on methodology. The majority view has become the consensus best practice – a national cap, with a possible fall-back to the worldwide ratio.

Australia has decided it will not implement the recommendations and, although the US would like further interest restrictions, it will need Congress to enact law, presumably as part of national tax reform. Many EU countries are likely to rely on their existing restrictions, based on domestic caps. The UK has not said publicly what it will do – but it would not be surprising if a consultation were published soon.

What next? We should hope that the expanded BEPS group, including developing countries, stays in place to continue setting the global tax framework. Only through this group working together is there likely to be cohesion to support common tax policies.