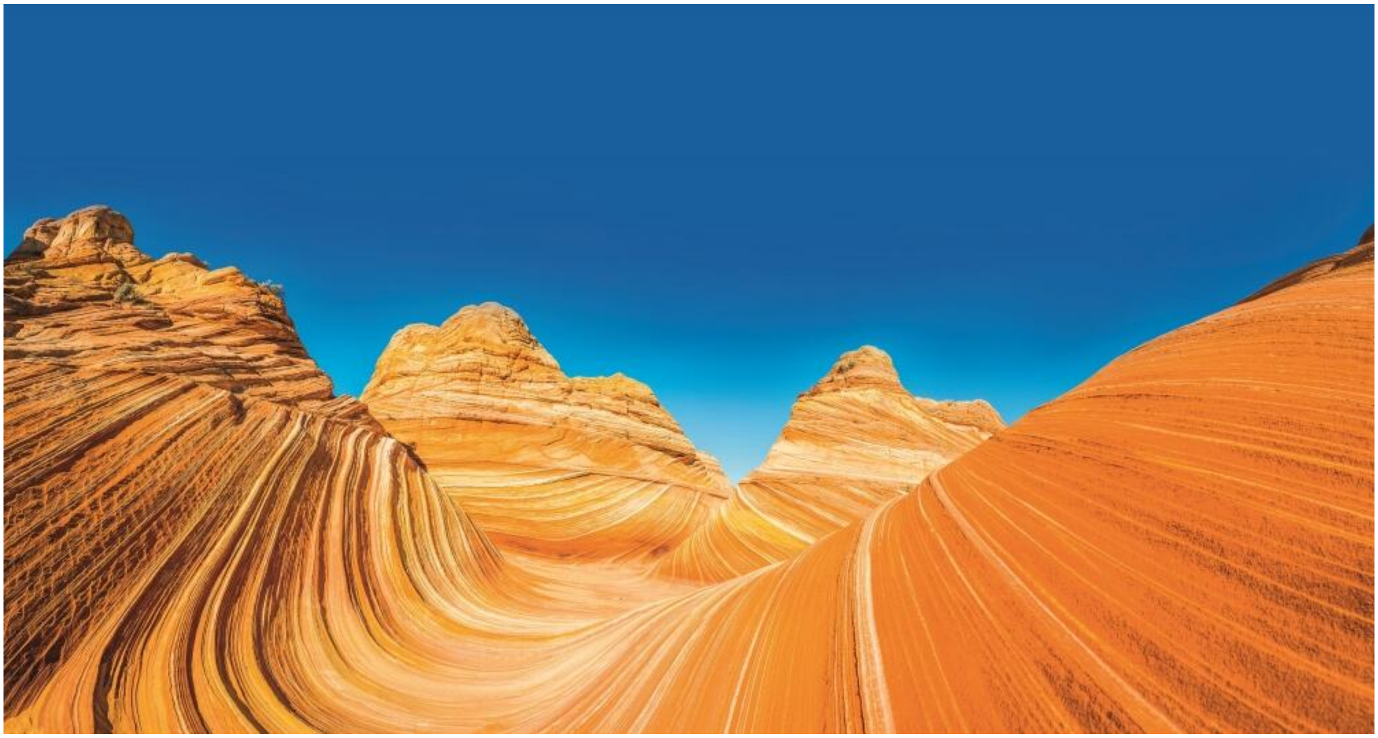
Continuing action

International Tax | Large Corporate



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Bill Dodwell provides an update on the Base Erosion and Profit Shifting project

BEPS Update

The G20 and OECD's Base Erosion and Profit Shifting project was put in motion by the G20 in November 2012. The project definition and goals were set out in February 2013 and the fifteen-point Action Plan published in June 2013. The first set of papers came out in September 2014 and the final thirteen papers covering all fifteen actions were published in October 2015 and approved by the G20 leaders in the following month.

What's happened since?

Perhaps the place to start is the October 2015 Explanatory Statement '…*estimates indicate that the global corporate income tax revenue losses could be between 4% to 10% of global corporate tax revenues, i.e. $100 to 240 billion annually…*'

The UK has moved to adopt domestic changes rapidly. Complex Hybrid Mismatch rules have been adopted in the UK from 1 January 2017 – ahead of any other country. The UK also plans on introducing limits on interest deductions, broadly as set out in Action 4, from 1 April 2017. The major changes to transfer pricing – which focus profits on people – started to be applied to UK cases from autumn 2015. The Diverted Profits Tax has reinforced the UK's position, at the cost of legal certainty. These changes – excluding the transfer pricing yield – have been costed by HMRC and signed off by the Office of Budget Responsibility as bringing in about £1.7 billion annually.

Given that UK corporation tax brings in about £50 billion annually, of which large company tax is about half, it seems that the UK is on track to add 10% to its corporate tax base for multinationals.

The EU has also moved rapidly to adopt anti-BEPS measures from 1 January 2019, with the introduction of the first Anti-Tax Avoidance Directive. This brings in a simple anti-hybrid rule (which negates the benefits of hybrids between EU countries), limits on interest deductions and CFC rules. More complex anti-hybrid rules will take effect from 2020 and 2022 (for so-called reverse hybrids). The EU is currently considering whether to propose Disclosure rules (Action 12).

Internationally countries are starting to adopt BEPS Actions. Countries such as Norway and India are making moves to limit interest expense. Australia and New Zealand are taking action against hybrids. Brazil has introduced disclosure rules.

The most wide-spread Action being adopted is for country-by-country reporting to tax authorities, under Action 13. All major countries have legislated for it, including the EU for exchange between Member States. The adoption of the new transfer pricing principles has also spread globally, with more than 35 countries applying them today.

The next major step was the establishment in summer 2016 of the Inclusive Framework. This is an open offer to any country to participate in the BEPS project on an equal footing – with the requirement that minimum standards must be adopted. To date, 52 countries and jurisdictions have joined the project, building on the original 44. Important countries such as Singapore, Nigeria and Kenya have joined jurisdictions such as Hong Kong, Bermuda and the Crown Dependencies. The G20 has encouraged the OECD secretariat to work with the IMF, World Bank and the United Nations to help middle and lower income countries adopt BEPS. The underlying objective is surely that the BEPS project will become the new global standard for corporate taxation. The EU has recognised this in designing its actions against non-cooperative jurisdictions. One of the requirements to stay off the blacklist is that the jurisdiction must have committed to adopt BEPS during 2017 and then pass the Inclusive Framework peer review. Peer reviews have become the favoured approach to policing adoption of global standards, as countries review each other and report publicly.

On 7 June the first signing ceremony for the Multilateral Convention takes place in Paris. 103 jurisdictions participated in the negotiation. Informal indications are that at least half this group will sign in June. Of course, the key step will be ratification, but signing gives a clear view to the business community of the direction of travel. The most important elements of the Convention are the changes to treaty abuse (which prevents an intermediary country being used to gain unintended treaty benefits) and dispute resolution, including optional binding arbitration. The first application of the new rules is likely to apply from 1 January 2018, but it will clearly take some time before all countries have ratified the changes. The OECD is optimistic that the Convention could prove to be a model for future treaty changes.

Finally, development of new standards continues. Discussion drafts on the allocation of profits to permanent establishments and the use of profit splits in transfer pricing are expected by the end of June. The first discussion draft on the transfer pricing of financial transactions will probably be released in July and guidance on the application of the treaty abuse tests is also due.

The G20 has also given the Digital Taskforce a new mandate – to review the digital economy and report by spring 2018, with a further report in 2020.

BEPS is no longer a two-year project; it has become the new approach to international corporate taxation.