BEPS Is Broader Than Tax: Practical Business Implications of BEPS

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Global tax rules are changing, and changing rapidly. The final reports on the Base Erosion and Profit Shifting (BEPS) Action Plan have been released by the Organisation for Economic Cooperation and Development (OECD) and endorsed by the G20. These reports on the 15 BEPS Action Points recommend significant changes in international tax laws and treaties. Due to the unique global alignment on the matter, BEPS is the most comprehensive change in international taxation in history. Attention has turned to the actions that are being taken by countries in response to these recommendations.

To succeed in this new, riskier environment, it’s critical to know how change will affect you. Our EY tax professionals will examine the impact of BEPS on key business functions and processes in the following nine chapters, addressing the various aspects of your global enterprise which may be affected by these changes.

This guide will provide readers with practical guidance on how to handle the implications of BEPS. Your approach to financing may have to change and your treasury function needs to be ready. Or, you may need to alter your operating model, as both multilateral and unilateral tax reforms will affect global business models and increase scrutiny of your business’s tax affairs. All company stakeholders need to be ready for more transparency. Global tax reforms could affect the value and structure of M&A deals; tax changes in relevant markets must be part of your due diligence. This shows that the impact of BEPS is broader than tax.

The demand for more tax transparency is building and you will soon be required to report information on what your business earns, and how much tax it pays, by country. That global information will be shared between governments and tax authorities, giving them new insight into your global footprint.

There are even calls to require public disclosure on this information. While this ‘public’ element of country-by-country reporting was not part of the final OECD recommendations, the European Commission is devoting additional time to assessing the merits of making such information public, as is being called for by many non-governmental organisations.

Are you prepared? The right strategy, processes and technology can help you manage this change.

We trust that this guide, BEPS Is Broader Than Tax: Practical Business Implications of BEPS, will provide you with deeper, practical insights into these complex topics and we hope you will enjoy reading it.
Is the use of holding and finance companies ‘inappropriate’?

Helmar Klink analyses various aspects of BEPS Action 6 and questions the changes the OECD hopes to make in absence of a proper economic analysis.

In the final report on BEPS Action 6: Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, the OECD alleges that multinational corporations (MNCs) deprive countries of tax revenues by claiming treaty benefits in situations where these benefits were not intended to be granted, such as by interposing holding and conduit finance companies. The OECD intends to put an end to inappropriate and abusive use of tax treaties through i) certain amendments to the OECD Model Treaty; ii) an amendment to the title and preamble of double tax treaties; and iii) outlining certain tax policy considerations for countries to reflect upon before entering into tax treaties.

It has been a long-held belief that corporations should be free to structure their affairs efficiently, as long as their arrangements are not artificial and abusive. This was well articulated in the 1929 case of Ayrshire Pullman Motor Services and Ritchie v IRC, where Lord Clyde said:

“...No man in this country is under the smallest obligation, moral or other, so as to arrange his legal relations to his business or his property as to enable the Inland Revenue to put the largest possible shovel into his stores.”

Much of the debate will revolve around the meaning of the word ‘abusive’. Is tax planning involving the use of tax treaties, principal companies, holding companies, finance companies and special purpose vehicles (SPVs) still allowed?

The fact that the OECD’s final report is not very final makes it difficult to go into much detail, other than the new principal purpose test (PPT) provision. In order to fill in the blanks left by the OECD, this article provides further guidance on how to apply the PPT provision in practice, starting with a short economic context, as this is critical for a proper understanding of the issues in play.

Economic analysis
Equity and debt funding should be better balanced
Since the beginning of modern corporate income tax (CIT) systems and the start of double taxation treaties, a discrepancy has been built into these systems in terms of the tax treatment of equity and debt. In a cross-border context, tax treaties could have provided a solution and could have restored the balance. Since dividends were distributed out of after-tax income, withholding tax (WHT) on dividends should preferably be zero. On the other hand, interest was typically allowed as a business expense in the source country. It would therefore restore the balance in the source...
country if payment of interest to an overseas lender incurs a fairly high level of WHT, say 20%. This way, there would be no incentive to fund overseas operations with (excessive) debt, there would be no reason for deferral, nor for conduit companies, since all foreign investors would incur the same high WHT in the source country.

Optimum allocation of economic activity
Economic theory explains that economic activity should take place where it is done most efficiently. In a world without borders, tariffs and WHT, we would arrive at the most efficient distribution of production and economic activity across the globe. Purely through the mechanism of price effects we would reach this state where our total combined global income is maximised. Double taxation creates obstacles that lead to a suboptimal distribution of economic activity, thereby slowing economic progress and reducing global income. The proposals in this final report will most definitely increase double taxation.

An incomplete report
The OECD has a reputation for solid research and argumentation. What is striking about the final report on BEPS Action 6, and atypical of the OECD as we know it, is:

- the lack of proof that MNCs pay proportionally less tax than small and medium-size enterprises (SMEs);
- the lack of consideration for and research into the balance between BEPS opportunities resulting from cross-border activities on one hand and inefficiencies (no offset for losses, non-deductible costs, non-creditable WHT, among others) due to cross-border operations on the other hand; and
- the lack of an impact analysis of the BEPS proposals on global trade.

After all, this is a report issued by the Organisation for Economic Cooperation and Development.

Principal purpose test (PPT)
Perhaps the most important and most hotly debated part of the report relates to the PPT. The final report on Action 6 leaves many questions unanswered. Most of the examples are very obvious and not instructive. This is an indication of the limited applicability of the PPT. Few examples provide useful insight, and where they enter the more interesting shades of grey, they reach the wrong conclusion. The analysis below attempts to answer some open questions and to provide better guidance under the PPT.

In the report, the PPT is article X(7) of the OECD Model tax convention and reads as follows:

“Notwithstanding the other provisions of this Convention, a benefit under this Convention shall not be granted in respect of an item of income or capital if it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of this Convention.”

Paragraph 5 of the limitation on benefits (LOB) test contains a different variation of PPT under the competent authority’s discretionary relief provision. See also comment 64 of the final report.

In tax law, a main purpose test or PPT is an established test to prevent abuse of a legal provision. Many countries have similar tests in their domestic legislation, or apply a general anti-abuse doctrine which is similar to the test proposed by the OECD. EU law has also adopted various provisions including a similar test and that operate as an anti-abuse rule. In the Cadbury Schweppes case, the European Court of Justice (ECJ) restricted the scope of specific anti-abuse measures to wholly artificial arrangements. Genuine business activities are protected by the EU’s fundamental freedom rights and will need to be respected.

The OECD’s PPT sounds rather ominous upon first reading, but should be read against the backdrop of a long list of case law in many OECD countries, and against the guiding principle of paragraph 9.5 of the Commentary on article 1 of the OECD Model Treaty:

“A guiding principle is that the benefits of a convention should not be available where a main purpose for entering into certain transactions or arrangements was to secure a more favourable tax position and obtaining that more favourable treatment in these circumstances would be contrary to the object and purpose of the relevant provisions.”

In fact, article X(7) is the codification of the concept of ‘fraus conventionis’ or abuse of law in an international context.

Many anti-abuse tests are part of the same family, but there are some interesting differences. First of all, the older tests refer to the “sole purpose” and the “main purpose”, whereas article X(7) speaks of “one of the principal purposes”. Apparently, the OECD intends to lower the bar and to make it easier for tax authorities to test the behavior of tax payers against the objective test. This has, however, no effect other than more menacing semantics, since all these tests end with the same objective test as the ultimate test. A second difference is that article X(7) provides a main rule and an exception to the main rule, instead of two tests of equal standing. Again, the optical effect is more threatening, but the final test is still the same.

A common feature of all these tests is that they first look at the purpose of entering into a transaction. This transaction needs to be connected with the actions of a person, typically the person claiming treaty benefits. Usually this involves an analysis not only of the apparent purpose of his action, but
TREATY BENEFITS

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His next 15 years were mostly spent overseas: he worked the Dutch desk in Paris for four years and in New York for six years. Since his return to The Netherlands in 2002, Helmar has shifted his focus to emerging markets in Asia, where he has hosted many of EY’s think tanks. His clients include governments, sovereign wealth funds, multinational corporations, private equity and real estate funds.

Two of his other areas of expertise are Curacao, where he functioned as treaty negotiator, and the sustainability of the Euro. Helmar leads EY’s Euro consulting team, combining macro-economic, legal and tax aspects. Helmar is also a member of the International Tax Committee of the Dutch Tax Bar Association (NOB).

EU guidance on PPT proposed by BEPS Action 6

Based on EU law it was to be expected that the EU would require anti-abuse provisions to be in line with existing EU law and case law. For this reason, the European Commission (EC) has issued a guidance on January 28 2016 with the following recommendation:

Where member states, in tax treaties which they conclude among themselves or with third countries, include a principal purpose test-based general anti-avoidance rule in application of the template provided for in the OECD Model Tax Convention, member states are encouraged to insert in them the following modification:

“Nowithstanding the other provisions of this Convention, a benefit under this Convention shall not be granted in respect of an item of income or capital if it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that it reflects a genuine economic activity or that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of this Convention.”

In other words, for EU countries the effect of the PPT proposal has been reduced to its legitimate proportions, as genuine economic activities will have to be respected.

The taxpayer’s purpose

An abusive purpose must be attributed to a person in order to be meaningful. From a legal perspective, it would be problematic to deny a certain treaty benefit on the grounds of another person’s abusive purpose. Tax law has not embraced a group concept; each company is dealt with individually. In other words, for the recipient of income to be denied treaty protection, it must be demonstrated that the recipient was party to an arrangement that had an abusive purpose. Merely being an associated enterprise does not satisfy that threshold. The objective of the recipient of the income must be assessed separate from possible motives of associated enterprises. If the recipient of the income has a clear commercial motive, grounded in its long term business plan, and was not aiming to realise an incidental benefit and is not party to a broader abusive arrangement, it seems extremely unlikely that treaty protection can be denied on the basis of another entity’s abusive purpose.

A genuine holding or group finance company may be established in a well-known financial centre. Provided this company has sufficient local substance to manage its assets, operations and associated risks, and notwithstanding that its management acts in close coordination with senior group management, they remain sufficiently autonomous. Such a company is acting in the ordinary course of its business; it is arguably not considered to have as one of its principal purposes the pursuit of foreign treaty benefits, and even if that were the case, such pursuit would be considered in accordance with object and purpose of the relevant treaty benefits. Consequently, such a company should be able to rely on the tax treaties concluded by its country of residency and tax benefits offered by the treaty partners.

In a way, the analysis boils down to what would remain in a ‘world without tax’. Genuine holding companies and genuine group finance companies would still exist as they have a
real economic function. Conduit companies, however, that lack a real economic function and carry no material risks, may not survive in a world without tax. Consequently, treaty claims from these companies may be in jeopardy under the OECD’s PPT, assuming the abusive purpose of their ‘principal’ can be attributed to the conduit company, which is no small legal step.

**Limitation on benefits (LOB) rule is not yet finished**

With the US being the biggest proponent of an LOB rule, the OECD is not able to proceed with final suggestions for its LOB rule as part of the rules to combat inappropriate treaty shopping under BEPS Action 6, as long as the United States has not finalised the work on its new LOB rule included in the US model tax treaty. The new version of the US LOB rule was released for public comment in May 2015, and was published on February 17 2016.

**Active conduct of a business**

The draft proposed LOB rule not only accords treaty protection to qualified treaty residents, but also to residents involved in the ‘active conduct of a business’ (ACB rule). To qualify under the ACB rule, the foreign income must be derived in connection with, or should be incidental to the business of the recipient of the income, and the latter business should be significant in relation to the business carried on in the foreign country.

Disappointingly, the OECD has resolved that headquarter companies do not qualify under the ‘active conduct of a business’ provision in the LOB rule published as part of BEPS Action 6. The commentary explains this with the argument that headquarter companies “manage investments”, as if it is a passive activity. In reality, headquarter companies provide active strategic and operational support to the underlying businesses of their subsidiaries. Hardly a passive ‘investment management’ activity. As the OECD’s comment is so detached from reality, it leaves the reader wondering if this is not politically inspired. (Interestingly, the recently published US Model treaty does allow treaty relief for HQ companies that exercise primary management and control functions).

In any event, it will result in double taxation on income that has already been taxed at operating company level (and triple taxation if ultimate shareholder taxation is included). Given the commentary, it is also unlikely that an HQ company can qualify for treaty relief via the proposed LOB’s PPT safety net, included in the discretionary relief provision (paragraph 5). This means that intermediate holding companies do not qualify for treaty relief if there is no significant local business. We wonder why the rules are drafted such that intermediate holding companies must be established in a large economy.

Smaller countries should not adopt the rules proposed by Action 6 (via the multilateral instrument of Action 15 or otherwise), as it will result in a brain drain and will exclude them from attracting higher tier corporate management teams. This could be resolved by considering business operations within a broader trade union. Moreover, it is probably illegal for an EU country to include the proposed provision in a tax treaty.

**Political or economic desirability**

It is a legitimate question to ask if the world should be longing for more treaty anti-abuse rules. Judging from the current media coverage on alleged inappropriate behaviour of MNCs, one would be tempted to conclude that at least from one corner of the political arena there is indeed a loud demand for stricter rules with respect to cross-border holding and financing structures. The OECD seems to provide these stricter rules by introducing this ominous-looking PPT, by stressing the first part of the test (one of the principal purposes) and omitting to explain the much more restrictive nature (for the tax authorities) of the second part (in accordance with object and purpose of the relevant treaty provision).

There is a negative feedback loop of incorrect, incomplete and mostly misleading information about tax planning by MNCs between mainstream media, politicians and public. Given the origin of some of this information, world leaders would be wise not to lean too much towards this political sentiment. Instead, they should give precedence to the urgent need for economic growth and the effect that additional trade and investment barriers will have on global trade and investment.
The impact of BEPS on financing and treasury

Shaun Lucey and Ariana Kosyan provide a comprehensive review of the way financing and treasury functions will be affected by Actions 2, 4, 5, 6, 8, 9, 10, 13 and 15 of the BEPS Project.

Financing and treasury (F&T) is a significant part of the OECD’s BEPS work, and is represented in eight of the 15 Action reports:

- The level of return that a lender is entitled to under transfer pricing (TP) principles as governed by Actions 8 to 10;
- The introduction of double taxation treaty anti-avoidance through the Action 6 and Action 15 reports;
- The cataloguing of international tax arbitrages in the Action 2 report, and a pathway for a domestic legislator to tackle these;
- Internationally coherent approaches to interest caps in the Action 4 report;
- Tackling harmful tax regimes through Action 5; and
- The documentation of significant F&T transactions in the master and local files recommended in the Action 13 report.

There is an underlying theme in tackling F&T BEPS, which is the lack of coherence of tax legislation in different countries. The thorny question is that, if tax law is made by domestic legislators, and approved by domestic governments, is it reasonable to expect territories to apply legislation consistently and coherently?

**Transfer pricing guidelines-based implementation**

**The impact of Actions 8 – 10**

From both a coherence and immediate impact perspective, this is the most significant part of F&T BEPS, as many territories automatically bring the transfer pricing guidelines (TPGs) into their domestic legislation. Our experience is that some tax authorities are approaching open enquiries as if the Action 8-10 report is a ‘clarification’ of the previous TPGs. It is definitely not this; it is a shift, and a fundamental one for F&T.

Actions 8-10 are aimed at developing TP rules to create TP outcomes in line with value creation. Specifically, Actions 9 and 10 target arrangements between associated companies which, in the mind of the OECD, enable BEPS by allowing inappropriate returns as a result of risk transfer, or an allocation of excessive capital to a group member, or by engaging in transactions that would only very rarely or never occur between third parties. If rules in line with the recommendations of BEPS Action 8-10 are adopted in local law (which in many countries will happen automatically), they will have a significant impact on the TP of both intra-group financial transactions and of financial entities.

The standard practice in most countries is to follow the contractual arrangements regarding the allocation of risk. What the OECD is suggesting is that tax authorities undertake a shift towards a world in which an overlay to contractual arrangements is postulated based on the ability of
and conduct of companies in relation to the control of risk. It can be expected that this will lead, in the short to medium term, to a great deal of confusion as different tax authorities interpret this overlay differently.

The updated TPGs focus on economically significant risk (ESR). According to the OECD, the significance of an ESR depends on the likelihood and size of the potential profits or losses arising from the risk and can be determined as a result of a broader functional analysis of how F&T value is created in a group.

The Action 8-10 reports suggest that once ESRs have been identified, it should be established which entity controls them. Controlling the risk requires having the capability of making decisions on taking or declining of an ESR bearing opportunity and on responding to the ESR together with the actual performance of that decision-making. If the entity contractually assuming the ESR does not control it or does not have the financial capacity to assume it, the ESR should instead be allocated to the group entity which factually does so. Where multiple entities exercise control over ESR and have the financial capacity to assume it, the ESR should be allocated to the entity (group of related entities) exercising the most control.

The TP treatment of capital-rich companies which fund risk-taking opportunities but have little other relevant economic activity (referred to as ‘cash boxes’) may be strongly affected. It is suggested that if such an entity does not demonstrate the control wished for by the OECD over its ESRs that the company exercising such a control has the right to collect the risk premium, and the cash box would be entitled to a risk-free capital return. This is one of the most difficult areas in respect of Actions 8-10, namely the suggestion that by operating a relatively low-activity company in a different manner could have a dramatic impact on return entitlement. This transfer pricing approach pierces the corporate veil, and is likely to create a great deal of confusion as different practitioners and tax authorities interpret it differently. It could also lead to double taxation and almost certainly increased controversy.

Many multinational enterprises have companies which undertake only financial activities. The transactions they are involved in may range from the provision of simple loans to more complex funding or the provision of guarantees, hedging and cash pooling activities. In the increasingly globalised business models of multinational companies leading to matrix management it, may be challenging to locate the person(s) actually exercising control over ESR as well as their location, which may sometimes deviate from the entity engaged in financing activities. These cases may become a target of Actions 8-10 along with cash boxes.

Given the far-reaching consequences of the Actions 8-10, groups should review their financing arrangements to ensure they are compliant from the TP perspective of the payer of financial payments, the recipient, and the recipient’s parent jurisdiction. Groups will need to monitor the approach of tax authorities in this area very carefully to understand the diversity of likely interpretations. It is surprising that, whereas most of the interest related actions promote and are designed to achieve coherence, an impact of Actions 8-10 could be less coherence – in the short to mid-term, at least.

**Treaty-based implementation**

**The impact of Actions 6 and 15**

Many jurisdictions levy withholding taxes on financial payments to protect their tax bases. In international financing arrangements, treaties generally promote the cross border flow of money through reducing these withholding taxes. Action 6 poses the question of whether bilateral tax treaties are being used by companies in the way that they were intended, and suggests that either a principal purpose test (PPT) or limitation of benefit (LOB) clause should be introduced into existing treaties to counter avoidance.

Action 6 also suggests draft amendments to the model treaty whereby the interest article (and other income articles) are restricted so as to only apply where the interest income is fully brought into account.

To ensure consistency and coherence it is suggested that a multilateral instrument would directly implement the treaty-related measures. The aim is to finalise this instrument and to open it for signature by December 31 2016, sign up to the multilateral treaty will be optional.

In general, these developments will create more incentives for source countries to start scrutinising financial payments made from their jurisdiction. The combined impact of Actions 6 and 8-10 will create a far more uncertain environment for cross-border financial payments, whereby the application of treaties and determining the beneficiary of financing profits may be open to alternative interpretations by different taxing jurisdictions.

This new lack of coherence may well lead in some cases to double taxation, and groups may need to redesign their F&T arrangements so as to minimise these risks. In particular as the positions of different tax authorities become clear, it may be that F&T arrangements become tailored to particular countries, rather than generic, as they largely are now.

**The impact of Action 2**

One of the fundamental principles of tax law in most jurisdictions is the deductibility of interest expenses for tax purposes where there are sound business reasons for this expense. The types of instruments or contracts that give rise to borrowing arrangements vary hugely depending on the circumstances of a particular group. As tax laws are different in each territory, there is no consistent approach to the taxation of borrowing arrangements. In the Action 2 report, the OECD postulates that this has created opportunities for groups to transfer profits from one jurisdiction to another through the use of interest deductions and other financial payments.

The OECD has demonstrated in the Action 2 report a detailed knowledge of the lack of coherence between different
country tax systems in this area (283 pages of examples). Its approach provides a way for each territory to legislate on a consistent basis so as to create coherence in this area.

At its heart, Action 2 requires a country to take into account the position of the taxpayer in the other country, and its tax treatment. To many countries’ tax legislators this is an alien consideration. They are concerned about the protection of their own tax base, so determining the tax treatment in their own country based on the treatment in another is traditionally something which has been shied away from.

It will be very interesting to see the extent to which different countries take this work on board. At the time of writing only the UK has published draft legislation to take forward the work in Action 2 into its domestic rules, to be effective for tax years beginning from January 1 2017. Territories such as France and Mexico introduced ‘half-way house’ rules during the OECD work, and it will be interesting to see whether they upgrade their legislation to be more detailed and in line with the OECD’s Action 2 final report.

An interesting development within the EU Commission is the proposal for an Anti-tax Avoidance Directive, issued on January 28 2016. The key thrust behind this draft directive is that the Commission believes that international tax avoidance can only be tackled by coherent action on behalf of its member states. The directive in many ways goes further than the OECD work on BEPS. However, in the area of F&T, its recommendations largely accord with the OECD’s Action 2 and Action 4 work. It will be interesting to see whether the EU member states will be able to agree on such a directive, as unanimous consent is required for a directive to become effective.

The impact of Action 4
In its report on Action 4, the OECD provides for a collective international approach to limit base erosion involving interest deductions and other financial payments. The recommended approach ensures that an entity’s net interest deductions are directly linked to its level of economic activity through the introduction of a fixed ratio rule based on taxable earnings before deducting net interest expense, depreciation and amortisation (EBITDA). In addition, a group ratio escape is introduced to align the deductible interest expense with the group’s consolidated external net interest expense. A country may choose not to introduce the group ratio rule, but in this case it should apply the fixed ratio rule to multinational and domestic groups without improper discrimination.

Due to the generic nature of the proposals, almost all groups would be impacted in one way or another as Action 4 would provide an overlay on what is an acceptable borrowing cost from both an internal and external perspective. If the external borrowing strategies of groups lead to non-deductible financing costs under Action 4 it will be interesting to see whether groups will adopt different strategies, such as borrowing externally into different entities.
Further technical review will be conducted by the OECD, which should be completed by the end of this year. So far, there are limited signs of jurisdictions replacing or supplementing their existing anti-abuse rules in relation to interest deduction with the Action 4 recommendations. Germany already has an Action 4-type measure in place. The Netherlands, meanwhile, has indicated that it will only support Action 4 on a coordinated basis, such as in an EU context.

As suggested above, the EU’s Anti-tax Avoidance Directive may also become important here. However, as with Action 2, it can be questioned whether countries will achieve consensus on the application of these rules due to different starting points, which is resembled in the wide variety of interest deduction limitation rules currently in place. It may be possible that (part of) the rules become optional. A country which has signalled the possible implementation as a result of initiating a consultation process on an Action 4-type rule is the UK.

**The impact of Action 5**

In Action 5 the OECD touches upon preferential tax regimes. In essence, the outcome of Action 5 is that preferential tax regimes require substantial activities. The OECD follows a so-called ‘nexus approach’, which requires that the economic activities are located in the same jurisdiction that provides the tax facility for these activities. Although the nexus approach is developed in the context of IP regimes, the same principle should apply to other preferential tax regimes, like financing regimes.

It can be expected that the nexus approach will become increasingly important over time, which is strengthened by an increase in transparency. Transparency is also a part of Action 5. In the report, a framework for the spontaneous exchange of rulings, which following the OECD could give rise to BEPS concerns, is provided. The spontaneous exchange will include rulings on financing structures that may be considered preferential and might not be considered in line with the nexus approach. This increase in transparency may result in more scrutiny towards existing financing arrangements and it can be expected that, over time, jurisdictions will act on this by closing down perceived loopholes.

Many jurisdictions have expressed their support towards the nexus approach and jurisdictions such as the UK, Luxembourg, Switzerland and the Netherlands have announced amendments to their IP regimes. In the field of transparency, the EU has taken a leading role with the ‘transparency package’, which was proposed by the European Commission in March 2015. As part of the package, a directive regarding the mandatory automatic exchange of information on tax rulings was agreed upon in October 2015. As of January 1 2017, EU member states will be required to communicate summaries of cross-border tax rulings and advance pricing agreements to all other EU member states and, within certain limitations, to the Commission itself.

**The impact of Action 13**

Action 13 contains provisions within the master file and local file for the documentation of significant inter-company F&T transactions, and the provision of rulings or agreements covering F&T. This Action is dealt with in a separate article but it is clear that due to its likely wide adoption by OECD states that F&T transactions will be available for inspection by multiple territories. It is therefore paramount that groups carefully and clearly document their F&T policies in anticipation of this, so as to reduce any follow-on controversy.
The impact of BEPS on the digital economy

Channing Flynn and Stephen Bates discuss the specific issues related to profit shifting in the fast-changing digital economy.

Digital economy taxation remains one of the most uncertain tax aspects of multinational business today. This is despite two years of work by the OECD on its Base Erosion and Profit Shifting Project (BEPS) Action 1: Addressing the Tax Challenges of the Digital Economy, and its recent work on related matters, such as indirect taxation, and also despite the public embrace of BEPS by national tax authorities that are rewriting their own policies and rules.

In fact, much of the OECD’s work on the digital economy lies ahead of it – delegated to its Task Force on the Digital Economy (TFDE) for completion in 2020. In the meantime, countries are implementing diverse national digital economy tax policies that reinterpret, and may even digress from, the new BEPS guidelines. In parallel, disruptive technologies and digital business models such as the sharing economy continue to evolve at a breathtaking pace that is exacerbating policymakers’ challenges.

With more and more companies and industries deploying new digital business models that disrupt traditional trade flows and strain existing tax regimes around the world, the OECD viewed its digital economy tax work as critical to the global economy – so much so that it was designated Action 1 of the BEPS 15-point Action Plan, which included the proclamation that “the digital economy is the economy itself”. Digital business was also implicated in the other 14 BEPS Actions: Action 1 guidance actually draws on Action 7 work on permanent establishment (PE), for example, and on other BEPS action items addressing controlled foreign corporations and harmful tax practices.

Now, with at least four more years of deliberation to come on some of the most difficult digital economy tax questions, tax uncertainty is among the biggest obstacles to doing business with the speed and agility necessary in today’s hypercompetitive global market. The current level of digital tax uncertainty acts as a drag on innovation, growth and profitability as it saps companies’ ‘digital confidence’. Think of digital confidence as the cross-functional grasp of the digital business catalysts of today and tomorrow, along with their tax, legal and policy implications. Digital confidence increases business foresight, from understanding the costs of doing business to predicting returns on investment and managing risk.

Companies now need to find the right framework to act with digital confidence in an uncertain environment (see table). From the financial services sector to life sciences and the technology industry itself, examples presented in this article illustrate the potential business impacts of BEPS. They are presented in the context of EY’s Digital Confidence Framework.
Digital confidence amid tax uncertainty

**EY Digital Confidence Framework**

<table>
<thead>
<tr>
<th>Grow</th>
<th>Optimise</th>
<th>Protect</th>
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<tbody>
<tr>
<td>Digital enterprise strategy</td>
<td>Digital incubation and innovation</td>
<td>Digital experience transformation</td>
</tr>
<tr>
<td>Digital supply chain and operations enablement</td>
<td>Digital risk management, cybersecurity, compliance, governance and audit</td>
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</table>

Companies across sectors need new strategies, business models and operating models purpose-built for a digital world.

Companies require cross-border agility in activating and managing their innovation processes and their portfolios of product, service, experience and business model innovations.

Customers are driving iterative and ongoing transformation in companies’ digitally enabled products and services.

Disruptive technologies enable new ways of manufacturing and distributing products and services, and new ways of running back- and middle-office operations.

Companies must master global tax compliance as one of the key risks in the regulatory and security mix of requirements.

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**Key OECD and BEPS tax changes in 2015**

The BEPS conclusion that the digital economy is the economy itself has digital tax implications for companies from all industries. Meanwhile, inconsistent national interpretations and implementations create global tax uncertainty.

The tax treatment of intellectual property (IP) will be subject to modifications in two key areas: the transfer pricing of intangible assets and risks, and the nexus provisions allowed under national IP tax incentives. 1 2

OECD guidelines to align all VAT and GST collection in the country of consumption are among myriad national and international changes to consumption taxes, requiring far greater attention by companies to pricing, digital interfaces and more.

The modified definition of permanent establishment regarding preparatory or auxiliary activities, plus anti-fragmentation rules, affects essential supply chain activities, including warehousing.

OECD-developed country-by-country (CbC) information exchanges give national authorities a greater cross-border view of companies’ tax profiles.

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**Some issues delegated to the TFDE report in 2020**

The OECD sees tax policy challenges evolving as the digital economy continues to develop, and these will be addressed in the 2020 report. Basics such as revenue characterisation are also up for further analysis.

The 2020 report is expected to incorporate new considerations from the next waves of digital business innovation, such as the sharing economy, 3D printing and others.

One proposal would tax value created by or attributable to individuals’ data, which is increasingly used to define content, marketing, services and the digital experience.

Further analysis will be carried out on physical versus ‘virtual’ nexus.

An ‘equalisation levy’ has been proposed on digital businesses operating in a country without being physically present.

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**Tax directors need to anticipate evolving tax policy**

As the OECD group responsible for addressing BEPS Action 1, the TFDE acted on the basis that technology is transforming how business is done globally and in every sector — how goods and services are sold, where companies base their operations and how they connect with their customers.

This transformation was seen as creating difficulties for governments’ tax authorities and sapping their national treasuries. For example, the mobility of intangibles puts pressure on the accurate administration of direct taxes on corporate income, while the mobility of customers puts pressure on the efficient collection of indirect taxes on sales. Another example is the ability of multinational companies to conduct substantial sales into a market from a remote location, with minimal personnel in-country. Such mobility engendered growing government complaints that multinationals’ organisational structures resulted in zero-tax, ‘stateless’ income — particularly when IP held in one country was globally commercialised in products and services.

A fundamental BEPS outcome is that “once the new measures become applicable, it is expected that profits will be

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2 EY Tax Alert: US proposed major changes to model tax treaty to counter base erosion. http://goo.gl/FfIC37
reported where the economic activities that generate them are carried out and where value is created”, as the OECD states in the Action 1 final report. Tax authorities will look to the development, enhancement, maintenance, protection and exploitation (DEMPE) functions surrounding IP within an organisation to analyse the global attribution of profits. This will challenge corporate tax directors to document the value drivers proactively throughout their global value chains.

Four recommendations are underscored in the Action 1 report:

- Modify the list of exceptions to the definition of PE regarding preparatory or auxiliary activities as they relate to a digital environment, and introduce new anti-fragmentation rules to deny benefits from these exceptions through the fragmentation of certain business activities;
- Modify the definition of a PE to address artificial arrangements through certain “conclusion of contracts” arrangements;
- Make a correlative update to the transfer pricing guidelines; and
- Make changes to the CFC rules addressing identified challenges of the digital economy.

The Action 1 report also reinforced recommendations developed outside of the BEPS process, such as a recent OECD regulation applying VAT and GST in the country of consumption and standard country-by-country tax reporting for greater global tax transparency.

The Action 1 recommendations were characterised as a first step in a long process of rewriting global tax policy for the digital era. A key BEPS project focus has been seeking better global alignment of companies’ profit attribution with the people functions of their business. Now, the TFDE will continue looking at the broader challenges of the digital economy, which include the possibility of a tax on nexus implications of digital activity, a withholding tax on sales of digital goods and services, characterisation of income from new business models, and the value created by, and attributed to, individuals’ data – all of which are expected to be addressed in a supplementary report to be released by 2020. (A detailed mandate for this work will be developed in 2016.)

Governments, meanwhile, are moving ahead, with a multitude of new VATs and GSTs (including, specifically, on digital services and low-value e-commerce transactions) and even with provisions that would establish ‘virtual PEs’ based on certain levels of digital activity in their country.

**Framing digital confidence**

As more people and businesses interconnect worldwide, as machines talk to machines in the “internet of things” and as the power of big data drives new business development, every enterprise needs a digital operating model. To attain digital confidence, companies must take a holistic approach to developing that model, strategically analysing tax along with other areas such as law, operations, technology and transactions across the five components of the model:

- Digital enterprise strategy;
- Digital incubation and innovation;
- Digital experience transformation;
- Digital supply chain and operations enablement; and
- Digital risk management, cybersecurity, compliance, governance and audit.

**Digital enterprise strategy**

Companies need to identify and deal with digital tax issues as early as possible in their business development processes, or risk creating unintended PEs, tax costs, compliance burdens, penalties, interest and reputation risks. This is a continuous engagement that recognises the value of agility in business as well as the benefits of ‘getting it right’ the first time when identifying opportunities, markets, pricing and profitability. It also recognises that, in the immediate wake of the final BEPS release, the level of uncertainty in these areas is driving risk to unprecedented levels.

For example, the financial services sector has seen a sharp increase in R&D related to new technologies. Many banks are investing in redeveloping core systems to allow mobile
access and are now increasingly offering niche applications as a way of targeting new customers. The creation of new IP and new mobile banking solutions may impact the bank’s domestic and international tax profile, including its existing transfer pricing.

In this example, tax directors at financial services firms can provide critical up-front insight into the BEPS theme of allocating profits in line with DEMPE oversight functions and their respective weight in value creation. By establishing profit split percentages in a given value chain, tax directors can provide a risk evaluation of the taxpayer’s overall transfer pricing system, quantify the benefits of various planning scenarios (IP planning, financing, restructuring, among others) and shore up documentation and tax compliance.

**Digital incubation and innovation**

Today, digital conveniences such as apps sit at the core of modern society and the global economy. As more data is being collected, stored and exchanged electronically, new opportunities arise, but so do new risks and responsibilities, including data privacy, data security and complex new relationships among the many players involved. The Action 1 report acknowledges this new reality, in projecting more work to come on individuals’ data, its potential value and taxation, to be completed by the TFDE in 2020.

In one example that confounds classic cross-border models, a global cruise-line recently wanted to “improve enjoyment” by providing guests on board its ships with digital mobile experiences. The internal IT team developed a next-generation commerce platform with rich, relevant and personalised content offerings operated from data servers on land, with the intent of increasing on-board spending. In addition to maintaining high levels of network and information security, as well as implementing measures to protect data privacy and intellectual property, the cruise line had to contend with the tax implications of cross-border and high-seas sales activity by citizens from multiple countries.

This example underscores how tax departments need to extract meaning from large volumes of data to meet their increasing direct and indirect tax obligations under BEPS. In particular, companies must understand the characterisation of new income sources, products and services. Forward-looking corporate tax directors may even want to be prepared to analyse value created from individuals’ data to determine the potential impact of a concept that would tax user-generated data.

**Digital experience transformation**

The digital revolution is changing the relationship that insurance companies have with their customers, the markets where they provide their services and the nature of the services they provide. For example, technology tools allow customers to bypass brokers and buy products directly from insurance providers. Consequently, insurance companies have developed digital infrastructure to replace certain processes that were once carried out by local personnel. And the ability to use remote servers to run complex underwriting algorithms means that contracts can be accepted by increasingly sophisticated software programmes.

In the post-BEPS world, tax departments within the insurance industry should consider the impact of this increased cross-border activity, how individual countries interpret this digital activity, and whether it may someday constitute a ‘virtual PE’.

**Digital supply chain and operations enablement**

In another case, a US-based insurer wanted to start providing warranty and indemnity insurance policies for a fast-growing global technology company. To calculate the correct tax, the company needed to obtain confirmation of the tax treatment of the insurance policies in 33 countries. This example illustrates the complexity of determining VAT, GST, stamp duty or insurance premium tax amounts to price the policies correctly. Most expect this complexity will only increase with the current wave of countries imposing new or modified VAT and GST. Adding to the challenge is the need to ensure remittance of the correct insurance taxes to the country where the risk is located.

**Digital risk management, cybersecurity, compliance, governance and audit**

Every company in every sector has to be aware of the OECD’s new CbC and master file reporting requirements, which are due as early as 2017 for 2016 financial data in countries adopting their use. The CbC initiative calls for
comprehensive global operational reporting by companies (including coverage of all locations, legal entities and branches of operation), to be shared among relevant countries via government information exchange mechanisms. Digitally enabled themselves, the standardised CbC reports are expected to usher in a new era of tax transparency, as underscored in the Action 1 report.

Tax directors should continually assess the systems and documentation needed, as well as their colleagues’ buy-in to the importance of averting reputational risk.

**Building digital confidence**

While it is hard to declare a ‘bottom line’ figure for the impact of BEPS, one can begin to extrapolate from the OECD’s declaration that governments worldwide are losing between $100 billion and $240 billion each year in tax revenue due to BEPS – or 4% to 10% of global corporate income tax revenue. The BEPS Project aims to redress these losses. Multinational companies also see the growing compliance costs in developments such as CbC tax reporting, the escalating information technology systems requirements for multiplying VAT and GST registrations and collection, as well as the potential business losses as tax uncertainty hinders new business development, and the potential reputational risk if found to be non-compliant.

Tax directors need to work closely with their counterparts across the enterprise to mitigate these negative impacts, align their company with the ongoing pace, complexity and volume of change in new multilateral and national taxation, and establish a digital framework to manage it all. Day-to-day operational issues will emerge. It could be that new product pricing should include a VAT cost not previously charged, for example, or that the leaders of a software development team need to work from an office in the jurisdiction of the IP owner.

Strategically, the stage must be set for success through a series of milestones: Action 1 implementation; the 2016 release of the TFDE’s new mandate for further digital tax policy development; and then the task force’s 2020 report on those policies. To achieve this, tax directors should:

- Actively track changes in digital economy taxation worldwide;
- Command a seat at the business strategy table; and
- Engage with national and international tax policymakers to facilitate rational digital economy tax policy.

Going forward, new frameworks, tools and analysis will be needed to re-evaluate the operating model throughout your global value chain, holding it up to OECD guidelines and their national interpretations in areas including IP alignment, CbC and master file reporting, possible risks of stateless income, double taxation, and the costly proliferation of PEs. Specifically, companies should take the following steps:

- Document the location of DEMPE oversight functions and ensure they align with attribution of IP profits;
- Convince your company’s business lines to include VAT costs as they develop product pricing;
- Alert the IT department to the risk that adding or changing data centres around the world could create new PEs in your global value chain; and
- Establish a dedicated committee to vet any short-term decisions affecting the development of IP and plans for global commercialisation.

All businesses want to operate with digital confidence. Given the current environment and heightened uncertainty in digital economy taxation, tax leaders can increase their level of confidence by initiating up-front and continuous planning across the enterprise – within a very deliberate framework that incorporates taxation as a matter of course.

EY would like to thank Jess Martin and Todd Scherzer for their contribution to this chapter.
The impact of BEPS Action 7 on operating models

Joost Vreeswijk and Ai-Leen Tan examine the impact that BEPS Action 7 will have on centralised operating models, and look at changes which multinationals should be considering to guard against exposure to the new rules.

For the past few decades, in search of lower cost and innovation, the majority of multinationals have steadily moved from a decentralised operating model – where functions (usually those relating to valuable activities of strategy and control) along the entire value chain occur in the same country – to one where certain functions, for a region or globally, are centralised in one country.

Whatever the business reasons are for these decisions, centralised operating models create cross-border business activities between related entities of multinational groups. Moreover, a move to a centralised model often has a negative impact on the profitability of the entity in the same countries where strategic or risk-bearing functions have been moved to a centralised location. In these situations, it is not surprising that tax authorities of such countries view such changes with some scepticism and assert that they are the result of base erosion and profit shifting (BEPS) measures taken by multinationals to minimise taxes paid in their countries.

To tackle this, the OECD’s BEPS Action Plan focuses on 15 key areas to ensure that profits are taxed where the economic activities generating those profits are performed and where value is created, while at the same time giving businesses greater certainty by reducing disputes over the application of international tax rules and standardising compliance requirements.

The action items deal with issues relating to the coherence of tax rules, substance of business arrangements and transactions, as well as the transparency of information disclosure by taxpayers to tax authorities about their cross-border business arrangements.

In this article, we will focus on the impact BEPS Action 7: Preventing the Artificial Avoidance of Permanent Establishment (PE) Status will have on centralised operating models.

Key features of centralised operating models

International operating models with certain centralised functions generally share the following key features:

• The centralisation of functions and risks in one location or legal entity (the principal).
• The central company (principal) is responsible for controlling key risks, performing strategic management functions and providing centralised services, such as procurement, product development and other support services, such as marketing, IT, HR, legal, accounting and finance, on a regional or global basis.
The ownership of all valuable intellectual property resides with the principal.

The principal operates its business by entering into contractual arrangements with local entities for the activities shown in Table 1. It is also possible for group entities to enter into cross-border contractual arrangements between themselves.

**PE issues associated with centralised operating models**

The main PE issue associated with centralised operating models is whether a PE has been created for the principal, due to:

- The activities of the local sales entity creating binding obligations (whether legal, economic or both) for the principal toward third parties;

### Table 1

<table>
<thead>
<tr>
<th>R&amp;D</th>
<th>Local entity operates as a limited risk contract R&amp;D service provider to the principal</th>
</tr>
</thead>
<tbody>
<tr>
<td>Manufacturing</td>
<td>Local entity operates as a limited risk toll or contract manufacturer for the principal:</td>
</tr>
<tr>
<td></td>
<td>• In a contract manufacturer scenario, the contract manufacturer buys raw materials, processes them and sells the finished goods back to the principal</td>
</tr>
<tr>
<td></td>
<td>• A toll manufacturer, however, buys neither raw materials nor finished goods; the principal owns the inventory physically located at the toll manufacturer’s premises throughout the production process</td>
</tr>
<tr>
<td>Sales and marketing</td>
<td>Local entity operates as a limited risk distributor or agent (either on a disclosed or undisclosed basis) with risks such as market, currency and inventory borne by the principal</td>
</tr>
</tbody>
</table>
Diagram 2: Identifying potential PE risk along the value chain

- The holding of the principal’s inventory at the warehouse of a local entity;
- The holding of the principal’s inventory at the premises of the local manufacturing entity;
- The activities of the local entity exceeding what is preparatory or auxiliary to the main business of the principal; and
- The activities of the principal’s employees who frequently travel abroad to do business or perform services on its behalf.

Diagram 2 illustrates the potential PE risk that can arise if the activities in blue are performed in a country that has adopted Action 7 changes to its treaties with the country in which the principal is tax-resident.

Before Action 7, the activities highlighted in blue generally did not create a PE because they were specifically excluded under the relevant article of the applicable double tax treaty or were structured that they did not exceed prescribed thresholds required to create a PE. Post-Action 7, however, these activities could create a PE, as the exemptions from PE status have been tightened and the thresholds have been lowered.

Action 7 proposes changes to the PE definition in Article 5 of the OECD Model Tax Convention (the OECD Model) to prevent multinationals from setting up arrangements that enable them to operate in another country without creating a PE. Action 7 will have an impact on the following aspects of centralised operating models:

- Commissionaire and similar arrangements (for example, sales agents);
- Facilities, such as warehouses, owned by the foreign principal used for storage, delivery or purchase of inventory;
- Inventory owned by the foreign principal held at facilities used for storage, delivery, display or processing (for example, toll manufacturing and consignment stock);
- Models where functions that could be seen as “complementary business activities forming part of a cohesive
“business operation” are carried out by group entities at the same or different place(s) in the same country; and
• Models where contracts for projects or services are allocated to, or performed by, several related group entities.

1. Commissionaire and similar arrangements
Commissionaire arrangements have long been the subject of much tax literature as to whether they create a PE for the principal or not. It is worth mentioning that, in the past few years, more and more tax authorities have been asserting that a PE has been created in their jurisdiction if a local commissionaire habitually enters into contracts that are binding on the foreign principal, even if those contracts are not actually in the name of that principal. Those commissionaires are, in their opinion, dependent on the principal.

Joost has designed and implemented numerous large scale change processes that focus on business streamlining, simplification and the implementation of central management companies, procurement hubs, supply chain companies, manufacturing footprint redesign as well as revised sales and channel management set-ups. Joost works across business, technology and tax disciplines.

There is no other country to which the activities described, however, will not create a PE for the applicable enterprise if:
• The activities are limited to the “preparatory or auxiliary” activities described in Article 5(4) as modified by Action 7
Or
• The activities are carried out by independent agents under Article 5(6). Here, Action 7 has modified the independent agent exception so that commissionaires that act exclusively, or almost exclusively, for the principal or closely related parties (defined as a party having more than 50% of the beneficial interest in the other party or of the aggregate vote and value of the other party’s shares) are automatically seen as dependent and will create a PE risk.

From a practical perspective, it will become more and more important to know not only how many days employees
spend in another country, but also what activities they perform while there. However, it will still be a practical problem for the principal to determine when a PE has been created, as Action 7 does not specify objectively how to measure whether the threshold has been exceeded.

Action 7’s changes to Article 5(5) mean that commissioner-aires that are not independent could now create PEs, even if their activities are limited to concluding or mediating standard contracts without active negotiation on their part or getting contracts formally (routinely) approved, signed or concluded outside of their country of operation without any material modifications. As long as the concluded contracts create an obligation for the principal to perform, it does not matter if the principal is undisclosed or that the contract is in the commissioner’s own name.

The management of cross-border sales teams will need to be more rigorous in future as it becomes more important to implement strict guidelines for how employees of both the principal and the local entity should act under the centralised model. For example, with respect to the authority to decide on pricing, discounts or changes to terms and conditions in order to manage PE risk.

2. Facilities owned by the principal for storage, delivery or purchase of inventory

Another area affected by Action 7 is the use of facilities for the storage, delivery or purchase of inventory by a foreign principal. Article 5(4) of the OECD Model specifically exempts certain activities from creating a PE where a place of business is used solely for activities listed in that paragraph.

Action 7 will modify the wording of Article 5(4) so that each of the listed exemptions from PE status is restricted to activities that are of a preparatory or auxiliary character, or the overall activity of the fixed place of business is of a preparatory or auxiliary character, taking into account the nature of the principal’s business.

This means that it will be necessary for businesses to check whether such activities constitute an essential and significant part of the principal’s core business. If so, it will not be considered preparatory or auxiliary, and will therefore not be exempt from PE status. For instance, procurement offices can now create a PE if the purchasing activity is considered to be an essential and significant part of the foreign enterprise’s activity. Taxpayers should note, however, that even if this activity is preparatory or auxiliary on its own, the anti-fragmentation rule could apply to overturn this exception (see discussion in 4 below).

3. Inventory owned by principal held at facilities used for storage, delivery, display or processing

As for situations involving principal-owned inventory held at a related or third-party warehouse, these may now create a PE if:

- The principal has unlimited access to the place where inventory is held for the purposes of inspecting and maintaining those goods (that is, it has the place at its disposal), or
- The inventory-holding activity is an essential and significant part of its overall business (that is, not preparatory or auxiliary).

Another common inventory-holding scenario that may now present multinationals with potential PE risk involves the use of consignment inventory arrangements where ownership of the consigned inventory placed at the premises of the customer remains with the principal. In such situations, the principal may need to re-evaluate its options for its end-to-end supply chain management, i.e. whether to keep the existing consignment inventory structure (bearing in mind that this may actually be a prerequisite to doing business in the other country for certain industries) or move toward a local inventory ownership structure (which has the drawback of making supply chain management more cumbersome and potentially inefficient).

Likewise, the same logic applies to situations involving principal-owned inventory held at a toll manufacturer for processing. Once again, even if the activity is preparatory or auxiliary on its own, the anti-fragmentation rule could apply to overturn this exception (see discussion in 4 below).

This means that the policies and procedures in place regarding warehouse or toll manufacturer access and stock control will need to be evaluated to see if they need to be modified to ensure that no PE is created, as if the principal has premises at its disposal, there is no further need to evaluate whether the inventory holding activity performed at this place is of a preparatory or auxiliary character.

4. Functions that could be seen as “complementary business activities forming part of a cohesive business operation” are carried out by group entities at the same or different place(s) in the same country

Perhaps the biggest impact of Action 7 is the introduction of an ‘anti-fragmentation’ rule to prevent the use of the Article 5(4) specific activity exemptions to avoid PE status artificially, such as fragmenting a cohesive operating business into several smaller operations in order to argue that each part is merely engaged in preparatory or auxiliary activities.

Previously, the activities performed at each place of business were viewed separately when determining whether or not a PE exists. In the future, all places of business will be viewed on a combined basis if the activities at these places can be seen as complementary functions that are part of a cohesive business operation.

If this is the case, the anti-fragmentation rule would apply so that the activities, when viewed on a combined basis, exceed what is considered preparatory or auxiliary, meaning that not all places of business will be able to take advantage of the exemptions in Article 5(4) to argue that no PE has been created.
The impact of the anti-fragmentation rule means that it will be more important than ever for multinationals to be able to substantiate the business reasons for allocating various functions and risks along value chains over different group entities within the same jurisdiction. Obviously, many multinationals have moved to functional specialisation and matrix structures where there is a deliberate separation of, for example, sales from manufacturing, or where manufacturing in one country focuses on producing similar products for multiple jurisdictions. These would appear to be logical reasons for the perceived legal and managerial fragmentation of key activities along the value chain.

5. Situations where contracts for projects or services are allocated to, or performed by, several related group entities

Action 7 also affects situations where contracts connected to the same projects or services are allocated among related parties and if the splitting-up of such contracts was done primarily to avoid PE status under Article 5(3). Under today’s rules, such situations do not create a PE because the contracts are allocated to related parties for durations shorter than the 12-month threshold prescribed under Article 5(3).

Going forward, the ‘principal purpose test’ (PPT) will apply to contracts allocated among related parties if they are connected to the same projects or services so that the 12-month threshold is exceeded and a PE is created. In these situations, multinationals will have to show that the principal purpose of splitting up those contracts was not to avoid a PE status under Article 5(3). This means that proper documentation should be kept as records of the main reasons (eg. commercial, regulatory or legal) for splitting up the contracts across several related parties.

Key takeaways

The impact of Action 7 on centralised operating models will have implications on the sustainability of existing operating models and the design of new operating models.

It will become more challenging for multinationals to find the right balance between risk management and control versus creating dependency in seeking to design an efficient operating model. There may be the need to re-evaluate the necessity of centralising certain key processes and functions, to perform a review of the roles and responsibilities relating to the management of those key processes and performance of those functions, as well as check where those roles are being performed and whether they need to be moved.

Improvements to the oversight, data collection and documentation of where people are, what they are doing and who they are doing it for will be key to assessing whether the existing operating model is robust enough to withstand PE risk challenges and whether there are opportunities for improvement.
The impact of BEPS on intangible assets

Sarah Churton, Ellis Lambert and Ian Dennis explain how the BEPS Action Plan is changing the tax landscape for intangible assets, and what this means for taxpayers.

The emergence of companies that rely on branding and innovation rather than physical assets and employee base to generate financial returns has created new challenges for tax systems that were originally designed to tax assets based on their legal ownership and physical location. Moreover, the physical barriers that often prevent multinationals from centralising tangible assets or an employee base in a jurisdiction do not inhibit the transfer of intangible assets in the same way, with multinationals able to divorce legal ownership and funding of intangibles from the activities that create or maintain the assets.

The commercial and legal drivers to consolidate ownership of a group’s intangible assets, and the tax advantages from doing so in a low tax environment, have resulted in the prevalence of structures designed to centralise the global or regional ownership of intangibles. While these structures are most common in technology, software and pharmaceuticals, they also often occur in other industry sectors, including consumer goods.

A central focus of the BEPS Action Plan has, therefore, been to identify and address the impact of these structures. The tax landscape for any group with intangible assets has changed as a result, and this chapter discusses the key implications of these changes.

What are intangible assets?
Intangible assets, by their very definition, are not physical in nature. Often, intangible assets comprise know-how that cannot be legally protected, but that nonetheless provides a sustainable competitive advantage. However, in some cases, intangible assets may be represented by legally registered and protected intellectual property (IP).

The definition of intangibles for transfer pricing purposes is a vexed question, and has been the subject of much discussion as the BEPS Action Plan has evolved. The final report on Actions 8 to 10 settles on the following definition, which is incorporated into Chapter VI of the revised OECD Transfer Pricing Guidelines:

“...something which is not a physical asset or a financial asset, which is capable of being owned or controlled for use in commercial activities, and whose use or transfer would be compensated had it occurred in a transaction between independent parties.”

The OECD notes that a definition that is either too narrow or too broad can be problematic, and has deliberately chosen a definition that does not rely on a typical accounting or legal interpretation. The OECD’s intent in presenting its definition is to provide clarity to taxpayers and tax
Intangible Assets

Diagram 1: Example of low-function IP owner

IP owner and parent company relationship
- IP owner has an exclusive right over the international IP rights outside of parent company’s jurisdiction.
- The entrepreneurial profit associated with the international IP rights accrues to the IP owner.
- While there is some substance in the IP owner, strategic decision making with regards to the worldwide rights remains in the parent company.
- The parent company does not seek to tax the income which accrues to the IP owner.

IP owner and local distributor
- IP owner licenses IP to a local distributor who makes sales to third parties in the local jurisdiction.

IP owner and affiliates
- IP owner enters into agreements with affiliates to provide R&D and other services applicable to the IP.

With this requirement for taxpayers to identify and document their intangible assets more explicitly, it is clear that there will be much more visibility in future for tax authorities on the intangible assets driving business value and taxable profit.

Key features of centralised IP ownership
Up to now, because legally protected IP has typically been easier to identify, value and transfer, it has often been the focus of multinational groups’ tax planning structures for intangibles.

While it is true that there is no ‘one size fits all’ IP ownership structure, it is often the case that tax-advantaged IP structures, to the extent that local country controlled foreign company (CFC) regulations did not prevent such structuring, have had the following features:
- Centralised legal ownership and funding of intellectual property assets (patents, trademarks and copyrights) in a single legal entity – the IP owner;
- Limited functional activity in the IP owner itself relating to the control or execution of IP development and management of resulting risk, whether by employees or the board of directors;
- Outsourcing of activity relating to the control and execution of development, enhancement, maintenance and protection of the IP; and/or
- Outsourcing of commercial exploitation activity to, for example, a local distributor typically in a higher-tax jurisdiction.

authorities, and it goes on in the report to give examples of the types of intangible that fall within this definition, including both intellectual property, such as patents and trademarks that can be registered, and other assets such as know-how, trade secrets and contractual rights.

It also notes that some factors that contribute to the income earned by a group are, nonetheless, not themselves intangibles. Group synergies and local market characteristics, for example, are to be treated as comparability factors in a transfer pricing analysis, not intangible assets.

The definition of intangibles contained in the revised transfer pricing guidelines is also referenced in the template for transfer pricing documentation contained in the Action 13 final report. These require that the transfer pricing master file transfer should present, among other things:
- A description of the group’s overall strategy for development, ownership and exploitation of intangibles, including the location of principal R&D facilities and R&D management;
- A list of the group’s intangibles, which are important for transfer pricing purposes, and details of which entities legally own them;
- A list of agreements including cost contribution arrangements, service agreements and license agreements;
- A general description of the group’s transfer pricing policies; and
- Details of any transfers of interest in intangibles undertaken.

With this requirement for taxpayers to identify and document their intangible assets more explicitly, it is clear that there will be much more visibility in future for tax authorities on the intangible assets driving business value and taxable profit.

Key features of centralised IP ownership
Up to now, because legally protected IP has typically been easier to identify, value and transfer, it has often been the focus of multinational groups’ tax planning structures for intangibles.

While it is true that there is no ‘one size fits all’ IP ownership structure, it is often the case that tax-advantaged IP structures, to the extent that local country controlled foreign company (CFC) regulations did not prevent such structuring, have had the following features:
- Centralised legal ownership and funding of intellectual property assets (patents, trademarks and copyrights) in a single legal entity – the IP owner;
- Limited functional activity in the IP owner itself relating to the control or execution of IP development and management of resulting risk, whether by employees or the board of directors;
- Outsourcing of activity relating to the control and execution of development, enhancement, maintenance and protection of the IP; and/or
- Outsourcing of commercial exploitation activity to, for example, a local distributor typically in a higher-tax jurisdiction.
Example of low-function IP owner
The existence and tax implications of this divergence between legal ownership and funding of IP assets from the functional activities relating to the development of the IP, seen in the typical low-functionality model described in Diagram 1, have been OECD’s key focuses in Actions 8 to 10 of the BEPS Action Plan. The revised transfer pricing guidelines set out in the final report seek to confirm that profits are allocated to the economic activities that create value using transfer pricing principles, with a focus on decision-making and control functions.

Why is tax a consideration when determining where to locate IP?
There can be many reasons why groups may choose to centralise their IP in a single location or company. Inevitably, tax often forms one of these considerations, with groups usually seeking to hold their IP in jurisdictions with:
- Low headline corporate tax rates;
- Tax deductions for amortisation of acquired IP;
- Reduced tax rates for certain types of innovative income (that is, a preferential IP regime); and/or
- Low or no withholding tax on royalties

Governments have recognised this trend, and have increasingly sought to modify their tax regimes to incentivise the retention and acquisition of valuable intangible assets.

This competition between jurisdictions has resulted in preferential IP regimes that enable groups to access low tax rates for IP income without locating significant amounts of IP development activity in the IP-owning entity. This level of competition has been deemed harmful by the OECD, which has made recommendations aiming to ensure that tax benefits are commensurate with the level of development activity performed by that entity.

These recommendations, which are contained within the final Action 5 report, clearly interact with the BEPS Actions that consider how transfer pricing principles should be applied to align profits with value creation. However, they seek to counteract separation of activity from IP ownership in a different way. Actions 8 to 10 focus on allocating IP profit to decision-making and control, while Action 5 focuses more strictly on aligning IP profit with the development activity itself. As discussed in the remainder of this chapter, the Action 5 and Action 8 to 10 changes all encourage groups to combine IP ownership, decision-making and control and development activity in the same legal entity.

The impact of BEPS on structures that separate IP ownership from decision-making and control
One long-standing criticism of the arm’s-length principle is that, in application, it may be used to place too much emphasis on the contractual allocation of business functions and risks, rather than on the activities responsible for value creation. This focus on legal contracts can result in transfer pricing outcomes where profits are allocated to low-function entities that do not have significant involvement in creating those profits.

While the newly revised guidance explicitly confirms that the contractual arrangements remain the starting point for a transfer pricing analysis, it places a clear emphasis on the commercial substance of transactions and the actual conduct and contributions of the parties involved.

Legal ownership and contractual allocation of risk achieves no more than a risk-free return
The revised transfer pricing guidelines set out in BEPS Actions 8 to 10 require the actual intra-group transaction to be accurately delineated and analysed to determine whether the respective functions and conduct of the entities are aligned with the contractual relationship. Where the conduct of the entities does not support the contractual relationship, the actual conduct of the entities takes priority over the legal contractual relationship, and the profits from the arrangements are allocated to the entity that makes the key contributions to the creation of these profits.

A functional analysis is used to understand the economically significant activities and responsibilities undertaken, assets used or contributed and risks assumed by the parties to a transaction in order to determine arm’s-length pricing. With respect to intangibles, particular attention should therefore be devoted to analysing the decision-making and control functions associated with the development, enhancement, maintenance protection and exploitation of intangibles that drive value creation in a business.

Crucially, the revised guidelines make it clear that entities that have only legal ownership of assets, or a contractual allocation of risk, should only receive a risk-free return under the arm’s-length principle, with supply chain profit allocated instead to those entities undertaking economically significant activities.

One-sided versus multi-sided functional analysis
In determining arm’s-length pricing, the revised guidelines emphasise the importance of understanding how value is created by the group as a whole, and the respective contribution of the parties to the transaction of that value creation.

A simple ‘one-sided’ functional analysis is unlikely to be sufficient to explain an entity’s contribution to value creation in all but the simplest of cases, particularly in the context of the enhanced transparency over a group’s entire value chain mandated by Action 13. Taxpayers will need to provide a more thorough analysis of functions, assets and risks, including consideration of the contributions of the transaction counterparties and the commercial context within which they operate.

It is not necessarily the case that this more rigorous analysis will inevitably lead to the increased use of profit split as a
transfer pricing method; in situations where the contribution of one party to the intra-group transaction can clearly be demonstrated to be routine, the use of a traditional transfer pricing method or the transactional net margin method will remain appropriate. What is true, however, is that it is likely to require more effort by the taxpayer to demonstrate convincingly that this is the case in a multi-sided transfer pricing analysis.

**Hard-to-value intangibles (HTVIs)**

Another focus of the new guidelines is to include specific guidance on HTVIs, to protect tax administrations from the negative effects of information asymmetry between themselves and taxpayers.

Examples of HTVIs are those that are only partly developed, or not yet commercially exploited, at the time of the transfer; intangibles where financial projections are highly uncertain and intangibles where reliable comparisons are not available.

The revised guidelines enable tax administrations to use *ex post* evidence on financial outcomes of an intangible transaction (i.e. information gathered in hindsight) as presumptive evidence of the appropriateness of the pricing arrangements.

The use of *ex post* evidence will be subject to safe harbours in certain situations. This includes cases where the taxpayer can provide reliable evidence that any variance between projections and the actual outcomes is due to unforeseen developments or foreseeable outcomes whose probability was originally estimated. Nevertheless, the ability of tax authorities to use hindsight to challenge taxpayers’ pricing assertions results in an additional layer of uncertainty and documentation requirements for taxpayers.

**What this means for IP structures**

The potential implications of the BEPS Action Plan for structures that allocate significant value to a low-function IP owner are obvious and stark. To address the increasing risk of tax controversy, adjustments and penalties, taxpayers should either reset transfer pricing policies to allocate profits to (higher tax) territories in which the economically significant activities take place, or redesign their operating models to align economically significant decision-making and control functions with IP ownership.

**The impact of BEPS on structures that separate IP ownership from performance of R&D activities**

The changes to transfer pricing guidelines do not impact the legitimacy of the outsourcing of functions such as R&D to related parties, provided that these functions are properly controlled by the IP owner and rewarded on an arm’s length basis. However, proposed substance requirements in preferential IP regimes may adversely impact arrangements whereby IP is beneficially owned by a different entity from the one that performs the R&D activity.

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**Diagram 2: Separation of IP ownership from R&D**

What is a preferential IP regime?

Many territories seek to incentivise the retention and commercialisation of IP in-territory, as well as the local performance of R&D activities.

They do this through both ‘front-end’ regimes, which focus on providing tax relief for expenditure incurred, and ‘back-end’ regimes, which apply to the income earned from the exploitation of the developed IP and are often referred to as patent or innovation boxes.

In the example shown in Diagram 2, a back-end IP regime may have historically been available to the IP owner in the territory where the entity is resident, regardless of the fact that it did not perform the underlying development activity which resulted in the creation of the IP rights. In addition, a front-end IP regime may also be available to the affiliates in the territory where they are resident.

**Overview of the OECD recommendations: the modified nexus approach**

The OECD’s final report on Action 5 defines parameters within which preferential IP regimes must operate so as not to be regarded as harmful tax competition. These parameters cover the types of IP which can be included within a regime and the method that must be applied to demonstrate that benefits are proportionate to substance.

**Qualifying IP**

Territories have historically taken different approaches to defining the scope of IP that can qualify for a preferential IP regime.

Action 5 requires a limitation of this definition to patents (under a broad definition) and copyrighted software that is the result of qualifying R&D.

Regimes that accommodate other IP, such as trademarks and trade names, will be required to amend their rules in line with the recommendations.
Substantiality requirement

The modified nexus approach seeks to create a direct nexus between the income eligible for benefits in a back-end preferential IP regime and the underlying activity that is performed on the creation of the IP.

Rather than applying the transfer pricing principles stated in Actions 8 to 10, the modified nexus approach uses expenditure as a proxy for underlying activity, limiting the income qualifying under a regime to the proportion of qualifying expenditure incurred by the IP owner.

Jurisdictions will provide their own definitions of qualifying expenditure. However, these definitions will be limited to expenditure that is incurred for the purposes of actual R&D activities. This is also likely to include the types of expenditure that would qualify for R&D tax credits under the laws of different jurisdictions, but not expenditure such as interest, building costs or costs not directly linked to a specific IP asset.

Substantiation formula

\[
\frac{\text{Qualifying expenditure incurred by IP owner to develop IP asset}}{\text{Overall expenditure incurred by IP owner on IP asset, including acquisition costs}} \times \frac{\text{Net income from IP asset}}{\text{Income receiving tax benefits}} = \text{Income receiving tax benefits}
\]

1. R&D outsourced to a foreign affiliate

Expenditure incurred by the IP owner on outsourcing of R&D to overseas related parties would not meet the definition of qualifying expenditure. This will be the case even if the activity is strategically managed by the IP owner.

However, the expenditure incurred on the related party outsourcing would fall within the definition of overall expenditure. Therefore, the related party outsourcing would adversely impact the nexus fraction shown in the calculation above and, consequently, the amount of income eligible for benefits.

Where parties other than the IP owners have performed underlying development, a restriction of benefits is likely to occur. This includes situations where affiliates have performed the underlying development activity but that activity has been under the control of, and funded by, the IP owner, as well as situations where the IP has been developed by another party (whether related or not) and then sold or licensed to the IP owner. Outsourcing of R&D to unrelated parties is not penalised, since this is treated as qualifying expenditure.

What does this mean for structures that separate R&D activity from IP ownership?

Below, the impact of the nexus approach in five different scenarios is considered. In each, R&D activities are separated in some way from either the entity, or the territory, that owns the IP.

1. R&D outsourced to a foreign affiliate

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Sarah is a member of EY’s international tax practice, where she advises on IP-related UK tax issues arising from acquisitions and disposals, investments into the UK, supply chain restructuring and IP centralisation. She has a portfolio of clients, both UK and US headquartered, with a particular focus on the life sciences sector.

Sarah has published articles in several tax journals and is a regular speaker at tax seminars and conferences. She is a chartered accountant and has a master’s degree in mathematics from Oxford University.

Ellis Lambert is a partner in EY’s transfer pricing practice based in London, with 17 years of experience, including two years working on EY’s UK tax desk in New York.

Ellis advises clients across a range of industry sectors on their strategy for intangible assets and on the design, documentation and defence of their transfer pricing structures. Ellis also leads the negotiation of advance pricing agreements (APAs) and MAP claims with tax authorities in the UK and overseas, as part of clients’ strategies for transfer pricing risk management.
2. R&D carried out by an IP owner in another territory
The OECD report does not include any requirements on the location of the R&D activity that is carried out by the IP owner. That means, for example, that the R&D activities of an IP owner’s foreign branches could give rise to qualifying expenditure. This is, of course, subject to the manner in which the recommendations are implemented into local tax law.

Where the IP owner has personnel carrying out R&D in foreign locations, the existence of a taxable permanent establishment and attribution of the IP owner’s profit to that PE would need to be considered.

3. In-country R&D
The separation of R&D activity and IP ownership between legal entities within the same territory would not appear to be contrary to the objectives that the BEPS project is seeking to achieve.

However, there has been concern within the EU that treating outsourcing of activity to related parties in the same territory differently from outsourcing of activity to related parties in another territory might be contrary to EU freedoms in some cases. Therefore, it is expected that EU IP owners will be equally penalised for subcontracting development activity to affiliates within the same territory as they would if they had subcontracted the development activity to a foreign affiliate.

As with scenario one, the related party outsourcing would adversely impact both the nexus fraction and the amount of income capable of receiving benefits. Therefore, this creates a potential incentive to combine R&D activity with IP ownership in a single legal entity.

4. IP developed by an affiliate and then sold to an IP owner
The Action 5 report sets out the basic principle that only expenditure incurred by the IP owner on qualifying development activity following acquisition of the IP would be capable of being qualifying expenditure.

Acquisition costs (including licensing fees and royalties) would, however, be included in overall expenditures. The Action 5 report explains that such costs act as a proxy for overall expenditures incurred prior to acquisition. This is despite the fact that such acquisition costs will likely include a return (sometimes significant) for the previous IP owner, over and above the costs of development it incurred.

Furthermore, in the context of related party acquisitions, these will be deemed to take place at the market value of the IP transferred, regardless of the consideration paid.

Therefore, in circumstances where the IP was substantially developed prior to being transferred to the IP owner, the nexus fraction is likely to restrict the income capable of receiving benefits.

5. Global R&D – cost sharing
Where several affiliates jointly contribute toward the development of IP and share in the rewards under a cost sharing arrangement, each of them will economically be an owner of the IP. In such cases, each entity’s overall expenditure will be equal to the amount that that entity contributes toward R&D expenditure. Where there is a mismatch between this amount and the physical contribution of R&D activity by the entity, the difference will be treated as related party expenditure, with a corresponding reduction in benefits.

This means that a cost sharing participant who funds R&D but does not carry out any R&D activity of their own will have a much lower nexus fraction than a company that both funds and carries out R&D.

Tracking and tracing compliance
Taxpayers that want to benefit from a post-BEPS preferential IP regime will need to track their cumulative expenditures in order to be able to substantiate the nexus between expenditures and income, and to provide evidence of this link to tax administrations.

In principle, this requires taxpayers to trace expenditure to each IP asset (that is, each patent). However, where such tracing would be unrealistic or would require arbitrary judgments, countries may allow taxpayers to trace expenditure to a product or, in limited circumstances, to a product family.

Regardless, this is likely to create an additional compliance cost for businesses that goes beyond the tax function, but focuses on the manner in which R&D personnel record their time.

Grandfathering and safeguards
The final Action 5 report confirmed that no new entrants should be permitted into an existing, non-compliant, IP
regime after June 30 2016. ‘New entrants’ in this context includes both taxpayers not previously benefiting from the regime and new IP assets owned by taxpayers already benefiting from the regime. A patent that is filed, but not yet granted, on June 30 2016, would not be treated as a new entrant.

However, for companies and IP already within a regime, jurisdictions are permitted to allow taxpayers to benefit from the existing regime until a specified abolition date, which may not be later than June 30 2021.

This means that companies should consider what steps they can take to gain access to the grandfathered regimes, which might include acceleration of patent filings. It should be noted that, to prevent a rush of multinationals transferring their IP into existing non-OECD compliant regimes before the June 30 2016 deadline, to avail themselves of the grandfathering period, an additional recommendation was made that grandfathering treatment should not be granted for IP that is acquired directly or indirectly from related parties after January 1 2016, unless such assets already qualified for another IP regime.

The additional transparency requirements will also apply to any new entrants into a preferential IP regime after February 6 2015. This will include spontaneous exchange of information on the identity of new entrants, regardless of whether a ruling is provided.

**Conclusion**

The combined effect of Actions 5 and 8 to 10 on IP structures is that multinational groups that wish to attribute substantial profits to an IP owner and obtain the benefits of a preferential IP taxation regime, will need to confirm that the IP owner carries out not only the funding of the IP development but also the decision-making and control over development, enhancement, maintenance, protection and exploitation of the IP, as well as a substantial proportion of the execution of the R&D activity.

Companies that do not to align decision-making and control with IP ownership will likely need to revisit their transfer pricing arrangements and can expect enhanced scrutiny from tax authorities where returns are considered not to be aligned with value creation.

Companies that do not align R&D activity with IP ownership will likely see the benefits available to them under preferential IP regimes reduced.

For all multinational groups, the changed tax environment creates the need to review their strategy for the creation, protection and exploitation of intangibles.
The impact of BEPS in M&A transactions

Adam Eagers and Mark Bennett look at the impact BEPS has had on the M&A market and discuss the commercial and operational aspects of any changes for investors.

The 2015 calendar year set a new record for global mergers and acquisitions (M&A) activity (by reference to the total value of transactions), driven by a series of megadeals, including ABI’s proposed takeover of SABMiller, Shell’s acquisition of BG Group, and Pfizer’s proposed blockbuster $160 billion takeover of Ireland’s Allergan.

Despite the growth in aggregate transaction value, driven by a wave of megadeals and particular strength in the US M&A market, deal volumes remain below their 2007 peak. However, the momentum in transactional value, coupled with growing levels of Chinese outbound activity (Chinese investors transacting abroad), as China rebalances its economy, could see the volume of transactions rise in 2016.

Indeed, respondents to EY’s 13th Global Capital Confidence Barometer indicated their expectation that the recent wave of M&A activity will continue – 59% of global companies noted they are planning acquisitions in the next 12 months. With the OECD’s BEPS Action Plan gaining significant momentum, this article looks at what BEPS – and the tax law changes it may bring – might mean for M&A transactions.

Specifically, we set out our views on the BEPS Actions we believe are most relevant in a deal setting; what BEPS means for investors commercially; how we expect transaction processes to adapt to the ‘new normal’; and what we are advising our clients to do now. To illustrate points, we generally refer to acquisitions; however, BEPS considerations are equally prevalent in disposals, IPOs, joint ventures and other capital market transactions.

The tax impacts of BEPS on M&A transactions

BEPS will impact on all aspects of the deal processes: due diligence; transaction structuring; and deal valuation. In the post-transaction period: impacting integration; compliance and reporting; as well as the operation and maintenance of structures.

In summary, we see the main interactions between BEPS and M&A transactions as being:

Value for financing costs
The transition towards single taxation under Action 2 (hybrid mismatches) and the tightening of relief under Action 4 (interest deductions) could reduce the value that can be accessed from transaction financing and foreign tax credits.
Treaty access
Professional fund investors, such as private equity (PE) funds, pension funds and sovereign wealth funds, may be impacted by Actions 6 (treaty shopping) and 7 (permanent establishment), at fund and holding structure levels, by restriction of access to tax treaties, requirement for increased levels of substance and ongoing maintenance of structures, and by the potential for fund management activities to trigger taxable presences.

Operating model flexibility
Trading companies will have their choice of operating models impacted, as well as the allocation of profits between functions and their ability to access to special tax regimes, such as patent boxes and other innovation supporting regimes, under Actions 8–10 (transfer pricing).

Transparency
Action 13 (CbCR) will lead to increased and complex compliance and reporting obligations, particularly for professional fund investors, with CbCR potentially required at fund, holding, management and portfolio levels, with consequent impact on costs.

Specific issues facing fund investors
- Tax transparency: we expect to see the trend towards greater tax transparency result in increasingly detailed information reported by funds to their investors.
- Substance in holding structures: we expect that holding companies will need to clarify how their management and decision-making functions meet wider commercial purposes. This may lead to increased costs of operating structures. We may also see PE groups withdraw from traditional ‘tax haven’ and low-tax holding jurisdictions that have sometimes included lower levels of substance.
- Caution with regard to beneficial ownership leading to reduced reliance on tax treaties: given the typical five-to-seven-year PE industry investment holding period, we expect to see a preference for transactions to be structured to access 0% WHT rates and capital gains exemptions where available under domestic law, rather than relying on the reduced tax rates available through tax treaties, until tax treaty changes are effected and taxpayers have more certainty as to how these provisions may impact their structures.
- Fund management activities creating permanent establishments: with the OECD definition of what constitutes a permanent establishment likely to broaden significantly, we expect to see certain activities that previously did not create a permanent establishment now doing so and therefore establishing a taxable presence.

What does BEPS mean commercially and operationally for investors?
Increased tax costs and uncertainty
With BEPS expected to increase tax costs for companies, and within fund structures, investors will need to assess the potential impact of how BEPS-driven tax law changes could affect transaction risks, structures and value.

A need for sustainable and durable structures
With years of potential uncertainty ahead, structures that follow single taxation are more likely to prove sustainable and durable when faced with revenue authority scrutiny – where investors rely on ‘less than single taxation’ structures, the ability to restructure tax-efficiently will be critical.

A downward impact on deal pricing
With higher overall levels of tax expected and an increase in the breadth of tax risks, a knock-on downward effect on deal pricing and investment returns appears inevitable – when divesting, investors who think ahead may be better placed to mitigate adverse pricing impacts.

A need to consider tax risk broadly
With reputational tax risk under increased focus by politicians and mainstream media alike, boards and investment committees will need to take a broader, non-financial and future-focused approach to assessing potential tax risks and costs – considering this also in the context of potential changes in regulatory and political environments.

A continual focus on maintenance
In areas of higher potential tax risk, in particular within fund and holding structures, investors will need to regularly assess whether structures are following their operating parameters.

Tax matters elevated in deals
These factors taken together indicate a need to increase the prioritisation and focus on tax within transaction processes.

What practical approaches can investors take to adapt to the ‘new normal’?
Understand and accept risk
Gaining an accurate estimation of a target’s future tax rate will become harder – this uncertainty may reduce the investor community’s confidence. Opportunities will arise for investors that can accept this risk and gain appropriate adjustments to purchase prices.

Understand and accept higher tax costs
Acquisition structures and operating models will be increasingly developed based on the core concepts of sustainability and durability – tax structuring to access less than single taxation may prove short-lived, and hence lead to over-valuation.
of transactional opportunities, and consequential low returns on investment. Investors who understand and accept higher tax costs need to be prepared to walk away from deals where the returns they seek cannot be generated.

Accept process complexity
The potential breadth of BEPS impacts expected in M&A transactions will add significant financial and operational complexities within the decision-making processes for investors. Factoring these complexities into deal time-lines, and having open channels of communication with tax teams, or moderating the need for certain detail, will be necessary to ensure that boards and investment committees are presented with the facts they need to make transaction decisions.

Look forward for risk
Tax due diligence may increasingly become future-focused as well as backward-looking, and include looking for risks that could arise under differing scenarios as to how countries will implement the BEPS recommendations into their domestic laws. As these uncertainties will continue to exist for a significant period of time, regularly reviewing risks and structures post-acquisition will enable investors to correct their course where needed.

Look broadly at risk
Risk assessments that take a broader view, rather than focus solely on financial impacts, will be demanded by boards and investment committees – this breadth will need to include reputational risk, and the risk of regulatory or political change.

Harness technology
As we have seen over the last decade, tax due diligence processes have adapted for new technologies – in particular, the use of electronic or virtual data rooms. We expect this rate of change to continue, with software used for data mining, benchmarking and analysis adding speed and value to deal processes. Consider for a minute this scenario: benchmarking tells you that your target company has a tax rate in the lowest quartile for its sector – do you consider this to be an optimised tax structure creating future value, or an indicator of aggressive structuring and therefore likely to leak future value?

Seek certainty where possible
with BEPS increasing uncertainty generally, we expect taxpayers generally to increase their use of APAs. In an M&A context, the reliance an APA can provide presents an opportunity for a seller to show where value exists; equally for a buyer, obtaining an APA can provide security of tax costs. Aligning deal time-lines and APA processes is an obvious challenge here, so we would expect sellers to be more proactive.

Plan for integration
As investors consider how BEPS will impact their existing operations (including holding structures, financing structures, IP and supply chains) on a stand-alone basis, they need to overlay how proposed transactions may impact on the existing business, and vice versa – for example, could the TP policy of the target, and its CbCR footprint, potentially undermine the current group’s carefully applied TP policy?
Reassess business operations

The increase in tax rates triggered by BEPS may, in some cases, undermine the financial performance of existing business units. Where they no longer meet their targeted capital returns, (hurdle rates), we expect some companies will start divesting businesses, or closing or scaling back activity.

What we are advising our clients to do now?

Essentially, from a tax technical perspective, it comes down to asking, and being able to answer, the following four questions:

- What are the historical BEPS risks within your holding and funds structures?
- What are the historical BEPS risks within your operating companies?
- What are the future holding and fund structures you need to put in place to be BEPS compliant?
- What targets are you looking to invest in or acquire? How could BEPS impact value?

But approaching BEPS is a wider challenge that tax technical aspects alone do not address. Our clients who are meeting the wider business challenges of BEPS, and taking them into account when executing M&A deals, are the ones who are best positioned to navigate the changing tax world successfully.

These challenges include:

- Communicating widely within their organisations the BEPS changes that are known and the likely direction of travel where they are unknown, and converting this into jargon-free business understanding; engaging in particular with legal, finance, treasury and business operations (including supply chain and sales leaders) and, of course, with boards and investment committees.
- Planning for change, understanding what might need to happen and when, the cost and resources needed for change and the likely impact on, and possible disruption to, the organisation;
- Being proactive in this area, and prioritising the time to think through potential implications under different scenarios; and
- Keeping a constant eye on the organisation’s reputational tax risk.

At EY, in an M&A setting, we cannot pretend to have all the BEPS answers, and to have done this all before – nobody can. We are helping our clients to think ahead and anticipate the future, in a commercial, practical and strategic way.

How we expect governments to react

- Introduce transaction reporting. We see the possibility that some governments will use Action 12 (disclosure of aggressive tax planning) to introduce transaction reporting procedures to enable the capture of data around fund flows, the acquisition of tax assets, commercial rationale for deals and to understand the tax effects of acquisition structuring.
- Aggressively target CbCR mismatches. We believe that the increased transparency driven by Action 13 (CbCR) will lead corporate investors to integrate and align TP policies of the companies that they acquire with their existing group policies more regularly, rather than seek to explain differences, which may not be apparent from the data provided under CbCR, to multiple revenue authorities that may be using financial metrics as a basis to determine when to raise tax audits.
- Dispute resolution. The agreed minimum standards under Action 14 (dispute resolution) are expected to have a positive impact for taxpayers in a deal context, with commitments to minimise uncertainty and the risk of double taxation arising for taxpayers, and reduce the time lines for resolving disputes. We expect governments who seek to attract foreign direct investment to commit to fund dispute resolution procedures, enabling them to provide a timely service to taxpayers who are transacting.
The impact of BEPS on tax compliance

Ronald van den Brekel and Tim Meijer analyse the compliance-related challenges which companies face, and how they can best allocate their resources to deal with them.

When the BEPS Action Plan was launched in July 2013, the OECD hinted at the purpose of these new measures and their potential impact on global tax compliance. While large multinational enterprises (MNEs) may have asserted that they are tax compliant today, this assertion may have to be reassessed due to the rapidly changing regulatory environment. An increased focus on tax and appropriate management of tax risks by tax authorities means MNEs will have to re-evaluate to what degree they comply with the tax rules of the countries in which they operate.

Based on the OECD recommendations in the final BEPS reports, many countries have started to make BEPS-driven changes to their domestic tax laws. Some Action Points will have an immediate impact on MNEs (for example, transfer pricing (TP) related topics, including Action 13 and Actions 8 to 10), while others require legislative changes to domestic tax laws or amendments of treaties in place (for example, Action 7).

Broadly speaking, the OECD’s recommendations will have an impact on the tax compliance process in the following ways. Firstly, through Action 13, a re-examination of existing global TP documentation is needed. Action 13 is primarily aimed at enhancing transparency for tax administrations by providing them adequate information to conduct TP risk assessments and evaluate other BEPS related issues. The new three-tiered approach (master file; local file; country-by-country report) will not only provide tax administrations with more detailed information regarding the global value chain of a company, but will bring inconsistencies in both TP policies and the implementation thereof to the surface. The increased documentation requirements, as well as other new mandatory disclosure requirements (such as those described in Action 12), will empower tax administrations across the globe to scrutinise the allocation of profit that results from existing TP policies within MNEs.

Actions 8 to 10 will place more emphasis on significant people functions and their relative functional contributions to key processes within MNEs. There is a clear shift in focus from the legal form to the economic reality of a transaction. In cases where the economically relevant characteristics of a transaction are inconsistent with the contractual terms, the actual transaction should be identified based on the actual conduct of parties. Contractual allocation of risk without sufficient control will not be regarded as arm’s-length behaviour, which has led to detailed guidance on analysing risks as an integral part of a functional analysis, including a new six-step analytical framework. In combination with the expansion of the definition of intangibles, this requires a thorough, two-sided analysis to
determine which party to the transaction is entitled to the profits related to these intangible assets.

Lastly, the impact of Action 7 is that the threshold for creating a taxable presence for corporate income tax (CIT) purposes in a country is lowered, with inventory holding, warehousing functions and sales activities being particular targets. As some of these proposed changes are already being implemented in newly negotiated tax treaties, the lower permanent establishment (PE) threshold will, among other things, impact how organisations will have to manage, monitor and report on their globally mobile workforce.

**BEPS impact assessment**

The BEPS Action Plan represents a fundamental change in international tax law and in the way tax administrations operate and cooperate. This means that MNEs need to change the way they organise themselves internally to reflect these changes in the external environment. The first step for MNEs to prepare for the increased compliance requirements is to perform a BEPS impact assessment.

Based on the specific facts and circumstances of a company, the key attention points are identified, based on the materiality and complexity of the transactions. In addition, the assessment should identify the specific jurisdictions in which they are doing business and that may be affected by BEPS. Subsequently, a detailed analysis of potential country specific impact areas should be performed. One of the main elements of a BEPS impact assessment is to determine whether additional resources are required (internal or external) in order to gather and provide the required information (for example, to meet Action 13 requirements). Ultimately, the impact assessment should result in a transition plan covering all relevant impact areas.

**TP documentation**

**Master file**

Multinationals should determine which departments (and persons) will be responsible for preparation of the new global master file. Subsequently, through a gap analysis, the main differences as compared to the existing documentation need to be identified. One of the starting questions is the strategic consideration what information to include in the master file, and what information to include in the local file. Companies should ensure the documents provided to tax authorities around the globe are consistent. Therefore, coordination between different regions when preparing the documentation will become crucial. The new guidance provides MNEs with several options, but at the same time creates quite some ambiguity. Specifically, the first year of preparation of a master file is crucial, as companies will have to make deliberate choices. One of these choices is whether to prepare the master file for the organisation as a whole (that is, in one single report), or whether to structure the documentation per business unit (where necessary with cross-references to other documents).

**Local file**

Similarly to the master file, companies need to decide which people in the organisation will be responsible for preparing the local files, and assess what the main differences are compared to the existing documentation, both from a process and a content perspective. Attention should be paid to the increased level of transactional details required, and how the financial data used in applying the TP method may be reconciled to the annual financial statements. Furthermore, searches for comparables will need to be updated every three years, and financial data on the comparables will have to be updated annually. In addition, the local file needs to be consistent with both the master file and the country-by-country reporting.

**Country-by-country reporting**

Country-by-country reporting (CbCR) has received a significant amount of attention during the BEPS project. This is not just because it is a new filing requirement which mandates an unprecedented level of global tax transparency, but also because it is a matter of urgency for multinationals. Following the BEPS guidance, many countries have amended their domestic law requirements, some of which have already come into force on January 1 2016.

According to the recently published proposed EU Directive, CbCR will be mandatory for all countries in the EU as of this date, even when the country of the ultimate parent entity does not require CbCR. This means MNEs will have to assess, at short notice, whether there are any risks or anomalies in their operating models that will show up in the CbCR (and the master file and local file), as it takes time for the necessary changes to be implemented. The focus on compliance with the new requirements will not only come from tax authorities in the countries that have already implemented new documentation requirements; the party auditing the financial statements of an MNE will ask for BEPS proof documentation during the course of their 2016 audit in order to perform necessary risk assessments. To be best prepared for CbCR, MNEs need to realise that the impact of BEPS is broader than the tax function. As a first step, it is recommended that the (internal) CbCR team consists not only of representatives from the tax department, but also includes finance and IT specialists.

The process to produce a sustainable CbCR process can broadly be divided into three main phases:

**Risk assessment**

Firstly, a high level risk and readiness assessment should take place to identify the availability of data and potential weaknesses in the tax structures or in control over certain (business) processes. An important element is to define early on in the process whether the tax and finance representatives agree on the data definitions required to eventually file the CbCR.
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Such a CbCR dry-run will, in our experience, likely produce ‘spikes’ in the data – some will be expected, and some will be more surprising. A true spike in the data simply reflects the reality of the operating model and tax structure. The dry run also enables you to identify so-called false spikes (for example, a year-end TP adjustment was erroneously booked in the wrong fiscal year). Based on all identified anomalies, a thorough mitigation plan and controversy strategy should be devised, including remediation of data issues.

Data collection process and impact on reporting systems
As aforementioned, global consistency between the various elements of TP documentation is important. The most logical way to achieve this is through a more centralised (global) coordination process. This starts with the data collection process, and the question of whether a company is capable of delivering globally consistent data. Multinationals should determine who is ultimately responsible for the data collection process. Ideally, the core CbCR team within MNEs will have tax, finance and IT capabilities.

Once the CbCR team is formed, one of the first steps is to jointly agree on the data definitions required for the CbCR process. There are often differences between the accounting entity hierarchy and the breakdowns necessary for CbCR. For example, consolidation systems frequently do not contain the results of sub-consolidations and, therefore, do not provide the detail by constituent entity necessary to compile the country-by-country aggregation. Similarly, at the entity level in the reporting system there may be embedded branches or PEs which will need to be broken down to provide data by jurisdiction.

As part of the assessment of the data collection process, a feasibility study of the existing IT and reporting infrastructure should be included in order to identify potential gaps in the existing systems. This study should link what kind of data (and from which sources) is required, and whether the existing reporting systems are ready to provide the required data. One of the key considerations is what sources of data to use (for example, group reporting GAAP, local GAAP or management reporting). In our experience, financial ledger data only will not be sufficient to produce a CbCR. Analyses early on in the process of the data definitions and of data availability are therefore important steps in planning for sustainable reporting.

Continuous monitoring
In this phase, MNEs should assess how to design checks and balances to perform annual (global) reviews as well as monitor the CbCR process throughout the year, including how to ‘certify’ the input data for the CbCR filing. BEPS will increase the focus on financial data, where the bridge between consolidated figures and figures recorded in final tax returns will be increasingly important. Such reconciliation is not required for CbCR, but tax authorities most likely will ask for it during audits.

Furthermore, in the local file, the reconciliation between statutory accounts and TP policy will have to be included. Many MNEs first prepare their consolidation, then finalise their tax returns in a second stage, with any discrepancies being corrected in the following period. This might not be a best practice in the new ‘BEPS environment’. The optimal position for the CbCR is to have system generated data without the need for manual offline workarounds. More (manual) workarounds will increase the risks of incorrect data. As tax authorities are becoming even more sophisticated in their ability to interpret data, tax functions within MNEs should probably be developing their own systems and processes. As an example, in order to timely identify potential anomalies, MNEs can monitor and test their CbCR output throughout the year, thus ensuring corrective actions.

Processes and systems should be enhanced to develop a sustainable approach to reporting. Once the CbCR is finalised, it should be checked to ensure it is aligned with the facts and circumstances as described in the master file and local file. In this final phase, MNEs should also consider how to create an internal documentation audit trail, as some questions from tax authorities may only come in a couple of years from now.
Permanent establishments (PEs)
The impact of Action 7 will be that the threshold for creating a taxable presence for CIT purposes in a country is lowered. As a result, organisations will have to manage and report on their globally mobile workforce. The remit of the new guidance is not limited to traditional secondees, but includes short-term business travelers, employees within MNEs who hold global and/or regional roles and project workers, as well as individuals employed under central business models.

With changes to the definition of a dependent agent PE being proposed, the number of cases where individuals may create a dependent agent PE is likely to increase. This may impact activities performed by senior executives, contractors and sales representatives, among others. It will be increasingly important to be able to monitor and track the activities of the globally mobile workforce, not only to determine where they are physically performing their activities, but also to understand thoroughly the exact nature of their activities. The next step is to increase awareness of the so-called ‘dos’ and ‘don’ts’ in order to educate MNEs and their employees on what activities they can perform, and which activities they should steer clear of in order to avoid unwanted PEs.

Under the new PE guidance, globally mobile employees within MNEs will likely lead to (potentially significant) PE risks. Failure to manage appropriately these PE risks associated with mobile employees may result in additional reporting requirements, penalties for non-compliance, corporate tax exposure, reputational risk and increased scrutiny from tax authorities.

Transfer pricing (TP) compliance issues
Many countries are expected to follow the guidance of Action 13 when updating their domestic TP legislation. This could, in theory, lead to a convergence in TP rules across countries. However, the reports use fairly general and broad language, which on the positive side has allowed more countries to agree with the recommendations, but on the other side can lead to differences in interpretations by individual countries. A possible outcome could be that rather than greater cohesion and consistency between national tax regimes, instead, we may see inconsistencies leading to more controversy and dispute. In addition, some differences in interpretation are already popping up (for example, some CbCR thresholds are in local currency as in Australia and UK), implementation dates differ, and additional exceptions may apply in specific instances, such as local file exemption for smaller companies in the Netherlands. To ensure that MNEs meet all the new local requirements, they should prepare a so-called dashboard to monitor compliance with local filing requirements across the globe. What may prove to be challenging in practice is that some countries will have informal requirements as well. Examples include jurisdictions that prefer local benchmark studies over regional ones, tax authorities that prefer to receive the documentation in local language, and more. All of these additional requirements and deviations from the main guidance may add to the complexity of meeting compliance standards in a timely manner.

Controversy
The rapidly changing regulatory environment has, among other factors, led to implementation of new domestic TP legislation, which will likely lead to differences in interpretation by individual countries. Enhanced transparency measures in combination with new mandatory disclosure requirements enable tax authorities to scrutinise the allocation of global profits within MNEs. While tax authorities have become even more sophisticated in their understanding of TP issues, these new measures will be complemented by increased tax authority resources and new tools intended to increase transparency. TP examinations have become more difficult and prolonged – a trend that is likely to continue.

More controversy expected
Fundamental changes and new rules subject to different local interpretation will create uncertainty for MNEs and, in all likelihood, lead to more controversy with tax authorities. This holds especially true in a transition period where countries may implement new rules at a different pace, and where part of the documentation that upon request may have to be provided to different tax authorities will be a translation of the document in original language.

In addition, the drive for increased transparency through automatic exchange of information (AEOI) will undoubtedly lead to more questions from tax authorities as they gain access.
to new sources of information, including CbCR. This, in turn, is likely to lead to more controversy. Lastly, when following the three-tiered documentation approach, additional details will need to be provided, especially in the local files, which may reveal some inconsistencies in the implementation of global TP policies.

Opposing views of tax authorities
Taxpayers are experiencing an external environment where tax administrations are facing demands to raise additional tax revenues as a result of the recent global economic downturn. In addition, through increased transparency, tax authorities have access to more information than ever before. In case this additional information leads to grounds for a different allocation of profits, such as in cases where a legal entity owning IP does not manage and control the key functions and risks, tax authorities may have opposing stakes in this discussion, which might increase disputes between tax authorities.

Structured controversy process
In order to be prepared in case of a tax audit, MNEs are advised to work on structured controversy strategies. Three main areas of attention should be addressed.

Firstly, in case of (local) tax audits, the division of responsibilities between central and local teams within MNEs needs to be clearly defined. To ensure consistency, it is advisable to have a communication protocol in place that requires local teams to inform the central team in a timely manner in a case of an audit.

Secondly, it is important to have a policy in place which determines who is responsible for gathering the relevant information in case of a tax audit, and who is in charge of monitoring timely submission.

Lastly, because of increased transparency between tax authorities, taking a position in one tax audit may have repercussions on other jurisdictions. Before taking such a decision, it needs to be clearly defined which persons with a holistic overview of the entire group are able to provide guidance, in order to safeguard an optimal outcome across jurisdictions.

Controversy strategies
As a result of increased regulatory uncertainty, advisers are experiencing a growing demand from MNEs for bilateral advance pricing agreements (APAs) in order to mitigate double taxation. In addition, Action 14 presents measures that aim to strengthen the effectiveness and efficiency of the mutual agreement procedure process in order to minimise the risks of uncertainty and unintended double taxation. They do so by ensuring the consistent implementation of tax treaties, including the effective and timely resolution of disputes regarding their interpretation or application through the mutual agreement procedure.

To manage controversy risk effectively, it becomes increasingly important for MNEs to design a robust controversy strategy, in which they develop a strategic approach to TP design, implementation, documentation, and defence. Being proactive can prove successful for limiting uncertainty, minimising the potential for significant controversy, and avoiding double taxation.

What lies ahead
As already witnessed in many OECD countries, the new BEPS requirements are being implemented in different ways and at a different pace. Whereas the initial aim was to achieve more uniformity, this may prove to be challenging, especially in the intermediate transition period. It is therefore important to thoroughly monitor which non-OECD countries will implement the BEPS guidance into their domestic laws. Furthermore, the proposed EU anti-BEPS Directive, published on January 28, 2016, will greatly influence the implementation of BEPS guidance into domestic laws of EU countries. Measures proposed in the Directive represent a minimum standard, which means that some local jurisdictions may introduce even stricter rules. Further work on the Directive is currently still underway, which means the final version may differ from the one published in January. Notwithstanding this fact, it is clear that there is a lot of momentum to further combat potential base erosion and profit shifting, which will in turn lead to a growing compliance cost for MNEs.

The implications for MNEs on their global compliance process are vast. Through an initial BEPS impact assessment, MNEs at a minimum need to assess whether:

- Additional resources (internal or external) are required to cope with the increased compliance cost;
- Internal processes need to be changed, including governance (clearly defining central versus local responsibilities), data gathering and monitoring of local regulatory developments;
- Re-examination of global TP policies and documentation may lead to a different allocation of profits;
- The tax, finance and IT departments are ready for country-by-country reporting; and
- The new guidance of BEPS Action 7 has created increased PE exposure.

The immediate impact of the BEPS Action Plan and increased transparency is that there will be more scrutiny from tax authorities and auditors regarding policies, implementation, and consistency. It is clear that a proactive BEPS impact assessment is a prerequisite for MNEs managing global tax risks, as time is quickly running out to remediate some of the inherent risks in their operating models.
The impact of BEPS on tax controversy

Monique van Herksen, Paul Mulvihill, Justin Liebenberg and Vikita Shah look at how BEPS recommendations affect tax controversy and dispute resolution.

The OECD’s BEPS Action 14 report presents measures that aim to improve the MAP process. The following analysis provides practical insight on what dispute resolution mechanisms may be available in the case of tax controversy for taxpayers, how they work and what pitfalls could and should be avoided in order to achieve rapid resolution of these matters.

Domestic dispute resolution options

Tax disputes usually originate from a review of the taxpayer’s filed tax return, published and public information, or information obtained otherwise by tax authorities. To manage a tax dispute, the appropriate amount of engagement with the issues being raised by the tax authorities is required. Multinational enterprises generally focus on global business opportunities and global tax impact. This focus may easily be misunderstood or misinterpreted as a focus on eroding a local country’s tax base.

Audit and settlement process

During a tax audit, several issues may be raised. Many of them can usually be resolved by providing additional information or explanation. If the information requested is not readily available locally, an appropriate response needs to be considered. If the requested information is sensitive or confidential, and the taxpayer does not have it or there is no approval for the taxpayer to disclose the information as it relates to associated enterprises, it can always be obtained via a formal exchange of information request under an available treaty.

In that case, a confidentiality agreement is likely to be applicable, thanks to the treaty mechanism. This may be challenging for countries that don’t have a wide treaty network – many developing countries, for example. If information is available or can be provided without internal complications, a swift response to the request will inevitably help overall with the preparation and resolution of the audit. It should be noted that some developing countries, such as South Africa and Kenya, have introduced rules that prevent the taxpayer from later using information to support their position if it was previously held back; this stops taxpayers from alleging that it is not possible to obtain information requested on foreign operations.

Once the tax authorities have received the requisite information, they will assess whether the tax return is filed correctly or an adjustment is required. In many countries, there is an opportunity to discuss facts and information with the relevant tax inspector and explain the position taken. This can help to resolve issues and close the audit. Most local country tax
In some instances, where an objection is rejected, there is a requirement for an administrative objection process to be followed. Tax audits can escalate. Misunderstanding, miscommunication, legacy issues and lack of trust can color the experience of the audit. Alternative dispute resolution mechanisms may serve to avoid this. They may be available through separate forums, where subject matter experts, unrelated to the taxpayer and competent tax inspector, review the issues raised, or where experts trained in negotiation and settlement techniques get involved.

Court-based adjudication of tax matters
The more traditional dispute resolution avenue is one where the taxpayer submits an appeal against an adjustment to an independent court of first instance. This avenue is generally a highly procedural one where, in addition to formal filings, statutes of limitations, filing fees and timely requests for extension of payment for assessments apply that need to be observed. Depending on the docket of the relevant court, it may take a long time before a decision is rendered. A decision by the court of first instance may be appealed to a court of second instance by either party. These courts will usually adjudicate based on facts and applicable law. The final competent court, or Supreme Court, usually only reviews issues regarding the correct application of the law. Some countries allow for independent review at the administrative level, after which a taxpayer has no further avenues to appeal the decision. Court-based adjudication does not guarantee avoidance of double taxation. This needs to be separately requested, within the applicable timeframe.

International dispute resolution
Increasing international trade and investment is accompanied by growth in cross-border commercial disputes. MAPs, APAs and international and commercial arbitration have emerged as preferred options for resolving cross-border tax disputes.

Mutual Agreement Procedure (MAP)
An MAP is an alternative dispute resolution mechanism available under most tax treaties. In a MAP, a taxpayer can ask the competent authority (CA) of its resident country to review the
The OECD started collecting this type of data. The figures show that, at the end of 2014, the total number of open MAP cases reported by the OECD member countries amounted to 5,423. This is an 18.77% increase compared with the initial 2006 reporting period, and a 130.57% increase compared with the initial 2006 reporting period, when the OECD started collecting this type of data.

Phase 1 – the competent authority process

The MAP article (Article 25) of the OECD model encourages resolution but does not necessarily make it mandatory to resolve double taxation. Taxpayers essentially have no international or treaty-based regress or action in cases where the CAs do not resolve a case submitted to them. Procedural rules apply. There is a time period within which an MAP request can be filed (usually three years) and a time period within which an MAP case should be resolved (usually a two years). There is some tension in the relationship between domestic measures (objection and appeal under national law) and avoiding double taxation under the convention via an MAP. However, as these two procedures usually do not go well together and one has preference over the other, Often, a domestic (one-sided) settlement impedes (full) MAP discussions, because the country of the primary adjustment may not wish to further amend a transfer pricing adjustment after having settled the case under domestic law. As a result, the other state may not provide for correlative relief. In some one-sided settlements, an explicit denial of access to the MAP process is even a condition to the settlement.

The above concerns have been addressed, to some extent, in the OECD’s final report on Action 14. The report proposes measures aimed at strengthening the effectiveness and efficiency of the MAP mechanism, such as specific actions to be taken by countries, suggested changes to legislation and administrative practices, and changes to the OECD Model Tax Convention and its commentary.

The report lists the main objectives of the measures as:

- To allow taxpayers access to the MAP process when the requirements for taxpayers to access the MAP process are met;
- To ensure that domestic administrative procedures don’t block access to the MAP process; and
- To ensure that countries implement Article 25 of the OECD Model Tax Convention in good faith.

A number of these measures constitute a ‘minimum standard’ for treaty-based dispute resolution, to which all OECD BEPS and G20 countries have agreed to adhere. The minimum standard is complemented with additional measures designated as ‘best practices’ to which only some of the OECD BEPS and G20 countries were willing to commit.

Phase 2 – the arbitration process

In 2008, the OECD issued an updated model including a major change to the MAP article (Article 25(5)) and added arbitration as an option for resolving double taxation. Arbitration under the OECD model applies to any person resident in a contracting state or, under Article 24(1) (discrimination based on nationality), to a national of a contracting state (if no avoidance of double taxation is achieved during the regular MAP process within two years), provided that the treaty between the contracting states contains an arbitration clause. States may limit the application of the arbitration clause to a more restricted range of cases, however.

Arbitration serves to resolve MAP cases swiftly if the CAs did not manage to reach an agreement during the two-year term they had to resolve double taxation. Generally, the procedure envisages that an arbitration committee is put in place to decide on the matter. Once a case goes to arbitration, the decision, when accepted by the person affected and by the respective authorities, has the status of a bilateral agreement resulting from the MAP.

Many countries still refrain from arbitration, however. This may be because the process is seen as one that leads to giving up tax jurisdiction to ‘outsiders’. The OECD BEPS Project and Action 14 report did not manage to achieve universal consensus to establish mandatory arbitration. Separately, however, 20 countries have committed to adopt and implement mandatory arbitration, however. Despite its reluctant acceptance so far, it is expected that mandatory binding MAP arbitration will be part of the negotiation of the multilateral instrument envisaged by Action 15.
Commercial arbitration for tax matters

Modern (commercial) arbitration has been promoted extensively by the International Chambers of Commerce to encourage foreign investment and offer a neutral and unbiased dispute resolution mechanism to foreign investors. Arbitration provides a way to resolve disputes between one or more unrelated persons, based on agreement of the parties and a decision that is general binding upon the parties.

Arbitration is offered and overseen via several organisations and forums. Commercial arbitration does not specifically cater to tax matters, and they are often explicitly excluded from commercial arbitration clauses. That said, in recent years, some tax matters have been eligible for arbitration, and the demand for resolution of tax matters by way of arbitration has increased. Commercial arbitration differs significantly from ‘conventional’ arbitration under the MAP process, however. The arbitration process is more akin to litigation than to the handling of a MAP request.

APAs

Of all the available options to resolve recurring international tax disputes, and in particular transfer pricing disputes, APAs are the preferred choice. Setting aside some of the challenges regarding accessing, administering, negotiating, and ultimately implementing APAs, these prospective (and often retrospective) arrangements are the most practical resolution to cyclical cross-border tax disputes. APAs are both cost-effective and timesaving, enabling multiple years of controversy to be resolved in one arrangement between tax administrations and taxpayers. Participating taxpayers obtain current and future tax certainty, while tax administrations can redeploy audit resources. Compared with other dispute resolution options, including the typical audit examination followed by normal recourse methods for disputed income adjustments, APAs provide opportunity for enhanced tax certainty and more streamlined compliance.

APA programmes have their share of sceptics in the international tax community, in particular with regards to timelines and results. However, APA programmes often attract the most complex and contentious cases due to the somewhat subjective nature of transfer pricing. As a result, due diligence and negotiation phases are often extended by a requisite period of time as taxpayers and administrations work through challenging and sometimes unconventional issues. If these difficult cases encounter lack of preparation and poor administration by APA stakeholders, that may convert a tough APA case into the equivalent of a long, forced uphill march. Nevertheless, APAs rarely go unresolved. The benefit of tax certainty and multi-year solutions outweigh most other considerations.

The following highlights from the Action 14 report specifically address how APAs may help advance the dispute resolution agenda:

APA rollbacks a minimum standard

APA rollbacks are classified as a minimum standard in Action 14 for those countries with bilateral APA programmes. Therefore, we can expect to see more uniformity and an increase in coverage of years as APAs will be expanded to cover prior years in more jurisdictions. Currently, taxpayers in some countries are required to lodge a cumbersome two-part request: one for a MAP covering prior years, and another for an APA addressing the prospective component. In some jurisdictions, the MAP and APA programmes are managed by different divisions or branches of the tax administration, often with different procedures and requirements. In these circumstances, APA rollbacks will certainly be appreciated.

APA rollbacks are currently a valuable and efficient feature of many bilateral programmes, and those programmes that have existing rollback policies should continue to develop improvements that promote uniformity in access and coverage of APAs.

Implementing bilateral APA programmes – best practice no. 4, publishing APA guidance – best practice no. 11

For counties that do not have a bilateral APA programme, Action 14 recommends establishing a programme and developing and publishing APA guidance as soon as they have the capacity to do so.

The growth of countries with APA programmes in the past fifteen years suggests that multinational enterprises (MNEs) will have the option to consider an APA as a dispute resolution mechanism in the future. Whether the existing APA programmes will be able to accommodate and process the expected influx of APA applications in a post-BEPS environment is still unclear. Upgrading the efficiency of existing APA programmes is as important as improving the underlying MAP process, since the more complex and contentious tax disputes are apt to find their way to APA programmes.
Although not specifically directed at APAs, the following concepts apply to MAP and, by extension, to APAs:

Access
Some countries consider APAs to be a privilege due to a perceived added benefit to taxpayers, either by avoiding an in-depth field audit or obtaining tax certainty for a future period. Due to this perception, APAs have been considered non-essential workload and have become less of a priority than MAP cases. More scrutiny has also been focused on an MNE’s ‘risk profile’ as well as on the intended covered transactions of a proposed APA to ensure the tax authorities approve of the approach before accepting the case.

Appropriate resources
Not only a sufficient number of qualified personal to assess, perform due diligence and negotiate APAs, but appropriate training on executing their competent authority mandate, are needed.

Improved processing time
Documenting the negotiations and finalising the APA through drafting and execution of agreements can be tedious and often a drag on the overall timeline of an APA. Binding arbitration is an essential component of Action 14 and should apply to most protracted disputes under MAP, including APAs.

What does the future hold?
The adage, “the only constant is change”, rings true with BEPS. The key elements of international tax and transfer pricing rules of five years ago are now dated. The overarching principles remain, but how we get there continues to change, and the OECD BEPS reports register a milestone in the progression of international tax rules. Globalisation and the recent economic climate have skewed policy development toward tightened rules and enhanced reporting and compliance requirements for MNEs. The only counterbalance in the new rules is Action 14, which seeks to improve the treaty dispute resolution mechanism.

The future will hold more scrutiny for MNEs across the board, resulting in a surge of international disputes. Without an appropriate response by governments through the implementation of Action 14, MAP and APA inventories will become overloaded, which might stifle trade and investment. At some point, MNEs may consider the cost of disputes so high that they adjust the way they do business in a country. The costs of tax disputes are eventually carried by individuals, who are end users and consumers of MNE-produced products and services, as MNEs invariably pass on costs to their shareholders or through the products and services offered. That may very well be the most compelling reason for tax authorities to take action and ensure that effective tax dispute resolution is available.

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How BEPS fits in with the EU’s tax agenda

Klaus von Brocke and Jurjan Wouda Kuipers look at how BEPS recommendations interact with EU tax laws.

The European Union (EU) has actively participated in the entire OECD BEPS process. It was represented notably by the European Commission’s Taxation and Customs Union Directorate-General (DG TAXUD).

In December 2012, ahead of the launch of the OECD BEPS initiative, DG TAXUD launched an initiative to address aggressive tax planning with the announcement of a set of immediate, medium- and long-term action points. Since then, it has continually worked through these points while trying to coordinate its own agenda with that of the OECD.

Alongside DG TAXUD, other Directorates-General – DG Market (transparency) and DG Competition (state aid) – contributed to the overall objective of reducing the phenomenon of BEPS. Furthermore, the European Council, with its Code of Conduct Group, as well as the European Parliament, came out with various initiatives to deal with the BEPS topic from an even broader perspective.

The following analysis serves to summarise and evaluate all stakeholders’ roles and functions and their respective initiatives against the background of the OECD BEPS Project. It also provides practical insights into what companies should focus on and monitor to be able to recognise, at an early stage, the need for potential changes to the way they operate within the EU.

The Council of Ministers
Ordinary versus special legislative procedure

The Council of the EU includes government representatives from all member states. It negotiates and adopts new EU legislation (based on proposals from the European Commission), adapts it when necessary, and coordinates policies.

When adopting legislation, in most cases, the Council decides together with the European Parliament through the ordinary legislative procedure, also known as co-decision. Co-decision is used for policy areas where the EU has exclusive or shared competence with the member states. In certain areas, however, the Council takes decisions using special legislative procedures where the role of the Parliament is limited.

This is the case with direct tax legislation that is adopted under a special legislative procedure where the Council votes unanimously after consultation with the European Parliament and the Economic and Social Committee (one of the EU’s specialised advisory bodies).
Code of Conduct 2.0
The Code of Conduct Group (Business Taxation) mainly deals with detecting and assessing potentially harmful tax measures that fall within the scope of the code of conduct (adopted in December 1997) for business taxation. It also oversees the provision of information on those measures.

Pursuant to the code of conduct, Member States have committed to abolish existing tax measures that constitute harmful tax competition and to refrain from introducing new ones in the future.

The code of conduct is not a legally binding instrument but its conclusions can have the power to exert a certain level of political influence, sometimes resulting in new legislation.

The Economic and Financial Affairs Council (ECOFIN), the legislative body of the European Union handling taxation composed of the economics and finance ministers from all member states, concluded, in December 2015, that the mandate of the Code of Conduct Group should be better used and strengthened. Among other things, the group has been asked to develop general guidance to prevent tax avoidance and BEPS activities.

Legal developments
Parent-subsidiary-directive (adoption of an anti-abuse rule (GAAR))
In 2014, the ECOFIN adopted an amendment to the Parent-Subsidiary Directive (PSD) to prevent the double non-taxation of distributed profits within corporate groups resulting from hybrid loan arrangements (loans that are considered equity for one party and debt for the other).

The PSD was originally designed to eliminate tax obstacles in the area of profit distributions between groups of companies in the EU, by abolishing withholding taxes on payments of dividends between associated companies of different member states and preventing double taxation of parent companies on the profits of their subsidiaries.

In addition, in 2015 the Council adopted a general anti-avoidance rule (GAAR) to be incorporated into the PSD. Both amendments have to be transposed into domestic legislation no later than December 31 2015.

Adoption of amendments to Directive on Automatic Exchange of Information regarding tax rulings and advance pricing agreements (APAs)
In December 2015, the ECOFIN unanimously adopted amendments to the Directive on Automatic Exchange of Information regarding tax rulings and APAs.

Member states had until December 2015 to implement the directive in their laws. The new rules will apply from January 1 2017. Under the revised directive, member states will be required to exchange information automatically on advance cross-border tax rulings, as well as APAs.

Shareholder Rights Directive and EU country-by-country reporting (pending)
In July 2015, the European Parliament adopted changes to a legislative proposal made by the Commission. Among other proposals, the European Parliament called for amendments to the Accounting Directive and the Shareholder Rights Directive, including an obligation for certain multinational corporations (MNCs) operating in any industry to report country-by-country (CbC) information on a consolidated basis in the notes to financial statements, including: turnover; number of employees; value of assets and annual cost of maintaining those assets; sales and purchases; profit or loss before tax; tax on profit or loss; and public subsidies received.

The same proposal called for public disclosure of information on tax rulings by a certain category of MNC.

European Commission
DG TAXUD (March 2015 transparency package and June 2015 action plan; EU anti-BEPS directive and common consolidated corporate tax base (CCCTB))
The European Commission represents the interests of the European Union as a whole (not the interests of individual countries). The Commission’s main roles are to propose legislation, and enforce European law, in that it is known as the guardian of the treaties. The Commission is divided into several departments: Directorate-Generals (DGs), and services. For tax matters, the most relevant are DG TAXUD (Taxation and Customs Union) and DG Comp (Competition).
EU PERSPECTIVE

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Jurjan Wouda Kuipers is a member of EY’s tax services practice in New York, where he heads the Luxembourg tax desk in the US. Jurjan frequently advises US multinationals on the tax aspects of centralising European operations, holding, financing or licensing activities in Luxembourg, as well as on the tax implications of pan-European acquisition strategies, mergers and joint ventures.

Jurjan has more than 27 years of experience in both Europe and the US. He has worked on a variety of international tax matters, including providing tax advice in connection with the structuring of mergers and acquisitions, cross-border investments and reorganisations, real estate transactions and cross-border financial instruments.

Jurjan is also the US-based representative of EY’s European Union (EU) competency group, a network of individuals from EY member firms who closely follow pan-European developments, such as state aid, the CCCTB proposal and European Court of Justice cases and their impact.

Legal developments promoted by TAXUD

Transparency (March 2015)

In March 2015, the European Commission presented a package of tax transparency measures as part of its agenda to tackle perceived corporate tax avoidance and harmful tax competition in the EU. A key element is the introduction of automatic exchange of information between member states regarding their cross-border tax rulings, including APAs. Other elements include assessing possible new transparency requirements for multinationals and reviewing the Code of Conduct on Business Taxation.

EU response and alignment initiatives to OECD BEPS (CCCTB) – new action plan

In June 2015, the Commission released a comprehensive action plan to reform corporate taxation in the EU. The plan includes revisiting the 2011 EU CCCTB proposal. The Commission advocated making the CCCTB mandatory and implementing it in phases (that is, postponing the work on consolidation until a common corporate tax base has been agreed). The revamped CCCTB should, among other things, eliminate mismatches between national tax systems and reduce the scope for harmful tax competition.

The ECOFIN has suggested that the Commission split the CCCTB proposal by carving out measures against aggressive tax planning from a future CCCTB directive proposal and integrating them in an EU anti-BEPS directive proposal. Hence, the Commission is tasked to deliver two packages of legislative and non-legislative proposals:

- New legislative proposals for a relaunch of the CCCTB project; and
- A separate anti-BEPS package of legislative and non-legislative measures.

Interest and royalty directive recast

The ECOFIN supports a recast of the Interest and Royalty Directive, which should include a GAAR.

Stand-alone EU Anti-BEPS Directive

In December 2015, the ECOFIN tasked the Commission to come forward with a package of anti-BEPS measures in the form of a stand-alone EU Anti-BEPS Directive. BEPS Actions 2, 3, 4, 6, 7 and 13 may be covered by this directive. Further analysis on technical details still has to be made. This hard-law approach will be accompanied by a soft-law approach. OECD anti-BEPS recommendations not covered in the EU anti-BEPS directive will be left to the member states to implement.

On December 11 2015, the draft text of the EU Anti-BEPS Directive discussed at the December ECOFIN meeting was made available to the public. The draft directive sets out minimum standards to which all EU member states would need to adhere. It includes a definition of permanent establishment, an interest deduction limitation rule, controlled foreign company (CFC) rules, as well as a GAAR and a hybrid mismatch rule.

The draft text goes beyond the OECD recommendations by including provisions on an exit taxation rule and a switch-over clause allowing countries to deny exemption of foreign income from permanent establishments under certain circumstances.

Although, the European Commission has responsibility for legislative initiatives, the ECOFIN can ask the Commission to put forward proposals that it considers necessary. It is unclear to what extent the legislative proposal to be put forward by the European Commission will mirror or differ from the current ECOFIN draft, or what the final directive will look like. However, it is clear that the implementation of this Anti-BEPS Directive in its current form will have a significant impact on the taxation of MNCs and may trigger an unprecedented change in European taxation.

CbCR Directive

Besides the above Shareholder Right Directive proposal’s suggestions on CbCR of information in relation to taxation, it is understood that the European Commission (DG FISMA or DG JUST) will make a CbCR of tax information proposal
Overview of current state aid investigations

<table>
<thead>
<tr>
<th>Country</th>
<th>Date of opening of formal investigation</th>
<th>Date of final decision</th>
<th>Subject matter</th>
</tr>
</thead>
<tbody>
<tr>
<td>Belgium</td>
<td>Feb 3 2015</td>
<td>Pending</td>
<td>Excess profit ruling system</td>
</tr>
<tr>
<td>Gibraltar</td>
<td>Oct 16 2013</td>
<td>Pending</td>
<td>Corporate tax system</td>
</tr>
<tr>
<td>Gibraltar</td>
<td>Oct 01 2014</td>
<td>Pending</td>
<td>Tax ruling practice</td>
</tr>
<tr>
<td>Hungary</td>
<td>Jul 15 2015</td>
<td>Pending</td>
<td>Food chain inspection fee</td>
</tr>
<tr>
<td>Hungary</td>
<td>Jul 15 2015</td>
<td>Pending</td>
<td>Tobacco sales</td>
</tr>
<tr>
<td>Ireland</td>
<td>Jun 11 2014</td>
<td>Pending</td>
<td>TP tax ruling</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Jun 11 2014</td>
<td>Oct 21 2015</td>
<td>TP tax ruling</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Oct 7 2014</td>
<td>Pending</td>
<td>TP tax ruling</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Dec 3 2015</td>
<td>Pending</td>
<td>(Foreign PE) tax ruling</td>
</tr>
<tr>
<td>Netherlands</td>
<td>Jun 11 2014</td>
<td>Oct 21 2015</td>
<td>TP tax ruling</td>
</tr>
</tbody>
</table>

Status as of Dec 11 2015

in March 2016. We could therefore potentially see three different EU interpretations of CbCR in 2016.

**DG Competition**

DG Competition is vested with special legal competence in relation to state aid law matters. It is regularly referred to as an EU-wide anti-trust regulatory body.

**Legal developments promoted by DG Competition**

State aid (pending or decided cases)

EU member states are generally not allowed to grant state aid to taxpayers. It is the task of the European Commission through its DG Competition to monitor compliance. DG Competition may open a state aid investigation if it finds out that a measure that could be considered state aid has been adopted without the Commission’s prior approval. If a company has benefited from a tax regime that is found to be unlawful state aid, it may have to repay the tax saved as a result of the tax benefit, plus (compounding) interest.

Since 2013, the Commission has been scrutinising various tax rulings and regimes. In relation to two rulings that had been issued to two MNCs by the Netherlands and Luxembourg, the Commission announced, on October 21 2015, its conclusion that the Netherlands and Luxembourg had granted illegal state aid to these MNCs. Both member states announced plans to appeal to the EU General Court and, ultimately, to the Court of Justice of the European Union, if necessary.

**European Parliament**

As regards the ordinary legislative procedure (co-decision), the European Parliament is put on an equal footing with the Council for the adoption of legislative acts. For special legislative procedures, the Parliament only has a consultative role. And, on certain subjects (taxation) the European Parliament can also only give an advisory opinion (the consultation procedure).

**TAXE**

The European Parliament formed the Special Committee on Tax Rulings and Other Measures Similar in Nature or Effect (TAXE committee) in February 2015. Its mandate was to review member states’ ruling practices. After months of public fact-finding hearings, the TAXE committee released a report that was adopted in a plenary session of the European Parliament on November 25 2015, by an overwhelming majority. The European Parliament, on December 2 2015, approved a measure to continue the committee’s work for six months under a new mandate.

**ECON**

The Members of the European Parliament are divided up into standing committees. Among other things, these committees instruct legislative proposals or amendments. After the November 2014 illegal leaking of Luxembourg tax rulings and public interest in the Commission’s ongoing state aid investigations, the European Parliament decided to launch the drafting of a legislative report on increasing transparency, coordination and convergence of corporate tax policies in the EU. On December 15, the European Parliament adopted a report with recommendations to the European Commission prepared by the ECON Committee. The Commission should now respond to the report, either by submitting a legislative proposal or by justifying why it decided not to honor the rec-
ommendations. The measures proposed in the report include EU-wide implementation of public country-by-country reporting for all multinationals in all sectors by the first quarter of 2016; expanding the scope of the newly adopted rules on automatic exchange of rulings and allowing the European Commission access to those rulings, as well as making certain information contained in the rulings public; a mechanism for member states to report to other member states and the Commission when they intend to introduce measures that could potentially constitute harmful tax practices; coordinating CFC rules; agreeing on a new approach to international tax agreements and tabling legislative proposals on hybrid mismatches, on a definition of ‘permanent establishment’, as well as of ‘economic substance’.

Evaluation and likely outcome

Given the multiple BEPS initiatives being led by different EU bodies, there are legitimate concerns that all of this work will ultimately create a very unsystematic approach to tackling BEPS, with all parties – the member states, the Commission, ECOFIN, the European Parliament and other stakeholders, such as tax campaign groups, having varying interpretations of how the BEPS Action Plan recommendations should be implemented in the EU.

It will therefore be more critical than ever that businesses closely monitor what has been decided, recommended and implemented (and by whom) in order to manage what will surely be a highly uncertain and complex year in EU developments.
Is your biggest tax burden the one you can’t see?
Taxes can quickly become prohibitive. Find out how we can help navigate your tax complexities at ey.com/tax #BetterQuestions

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The better the question. The better the answer. The better the world works.