

Global Tax Policy and Controversy Briefing

Issue 21 | February 2018

The EY logo consists of the letters 'EY' in a bold, white, sans-serif font. A yellow triangle points upwards from the top right corner of the 'Y'.

Building a better
working world



"You see just by opening newspapers that there is an intense focus on the taxation of the highly digitized world ...

... there is a significant political impetus – certainly in Europe, but also beyond...

... there is a desire, and a political will, to go beyond purely consumption tax solutions – to seek ways of adjusting what is perceived as an imbalance on the basis that if we were to draft the rules today, we would probably draft them differently."

*– Interview with
Achim Pross, Head
of the International
Co-operation and
Tax Administration
Division, OECD
Centre for Tax Policy
and Administration*

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WELCOME

And so, it has finally happened: whether you saw it as an early Christmas present or a year-end tax accounting headache, US reform has been signed and sealed, and it is now down to the rest of us to see just what it means for business – and also for governments elsewhere, who will have been avidly assimilating the final details and wondering what it means for their own tax competitiveness.

President Trump on 22 December signed the “Tax Cuts and Jobs Act” prior to leaving Washington for the holidays, sealing the most significant legislative achievement to date of his Administration and the first major overhaul of the federal income tax in more than 30 years.

The final conference agreement that became the signed Act reflects compromises by the conferees in a host of areas, including a 21% corporate tax rate that will be effective in 2018 – up from 20% in the bills passed by the House and the Senate – and a 37% top individual income tax rate that would apply to joint filers with annual incomes over \$600,000.

The deemed repatriation tax rates for the transition to a territorial tax system were eventually set at 15.5% for earnings held in cash or other specified assets, and 8% for the remainder. Slightly higher than the earlier drafts. Additional cost-saving changes were included that mean that the Act results in a net tax cut of \$1.456 trillion over 10 years.

For full analysis of all provisions of the Act, readers are recommended to access EY’s US tax reform pages at:

ey.com/taxreform



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The successful enactment of US tax reform may spur action in two related areas; first, a 21% federal corporate tax rate effectively drops the US to *just* below both G7 and G20 averages (when average state taxes are added), and policymakers will be assessing the competitive implications and potentially assessing how to drive tax competition while staying within the constraints of the BEPS recommendations. Possible reactions include further corporate tax rate reductions, enhanced incentives and the possibility of a new withholding-tax led era of competition. Our *2018 Tax policy and controversy outlook*, out in February, provides some early indications on this front, indicating a distinct acceleration in the number of countries improving or even creating new R&D incentives.

Second, clearing the hurdle of tax reform may well put the focus more strongly on the debate on the taxation of digital activity. Here, as our article on page 15 describes, September and October 2017 in particular saw a flurry of activity from a range of national and multilateral stakeholders, with much of the focus being on European Commission activity. As our article notes, the heart of debate in Europe focuses on two core issues: whether the consensus position developed within BEPS Action 1 – namely that there is “no such a thing as a separate digital economy, but that companies are now participating in the digitalized economy” is sustainable, and that the overall timeline for action – thus far a timetable set by the OECD – should not only be brought forward, but should also include far more focus on the division between source or “market” and residence taxation.

As we move further into the year, attention will focus on proposals to be put forward by the European Commission in this area. It is likely they will follow a two-phased approach – a short term equalization levy, potentially, perhaps followed by a more permanent nexus change designed to usher in the long-debated Common Consolidated Corporate Tax Base. With the OECD set to release its own recommendations in April, this is set to be an interesting start to the year.

MLI

The new year also saw new activity in regard to the OECD’s *Multilateral Instrument to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting* – or “MLI.”

As Pascal Saint-Amans, Director of the OECD’s tax unit told EY’s International Tax Conference in October, “by mid-2018, the MLI will cover around 100 jurisdictions. And in 2019, we will be able to identify who is playing by the rules and who is not.”

This indicates that the OECD expected a further 30-or-so jurisdictions to sign the MLI at a ceremony in Paris in January; in fact, only six did, with a further four expressing their intent to do so in the future. Many others are expected to sign during the course of 2018, and even as of today, some 1,200 tax treaties are expected to change as a result.

With two signing ceremonies now behind us, trends (and outliers) in country approaches can be identified; for example, nearly two-thirds of signatories chose for the terms of the specific activity exemptions (in relation to permanent establishment,) to apply. On the other side of the coin, though, 24 of the 68 signatories said that they intend to meet the minimum standard for improving dispute resolution outside of the MLI. That is a disappointing figure. Page 30’s article provides some further analysis.

Searching for certainty

The OECD, meanwhile, remains keen to try and stem the number of disputes from rising, while also trying to ensure that tax administrations are provided with the best available tools. As Ronald van den Brekel describes on page 27, this includes recently making their *Country-by-Country Reporting: Handbook on Tax Risk Assessment* available publically. The handbook contains 19 specific risk factors, which in turn effectively represent the types of analytics test – at a minimum – that national tax authorities will be employing. “While it might not provide a complete picture,” says Ronald, “the OECD handbook nonetheless provides useful guidance to those companies wishing to develop pre-submission tests to ensure their compliance risk assurance approaches are aligned with those likely to be adopted by the tax authorities – presumably exactly what the OECD is hoping.”

2018 is already shaping up to be yet another busy year. We hope you are able to make the best of what it offers.



The interview: Achim Pross – Head of the International Co-operation and Tax Administration Division, OECD Centre for Tax Policy and Administration

Marlies de Ruiten, EY Global International Tax Services Policy Leader interviewed Achim Pross at the OECD's Paris offices in October, 2017.

The full interview, in both text and video form, is available at ey.com/tpcbriefing

Marlies de Ruiten: Achim, I'd like to start with the peer reviews, and the minimum standards. The first minimum standard that is being peer reviewed is the one on dispute Resolution, on MAP. The first reports have been issued; the countries involved are all countries that are generally considered as quite "good" countries. Were there outcomes that surprised you in these reports, in the outcomes of the peer reviews?

Achim Pross: By and large, they were as expected. We didn't have big surprises. We have, I think, about 50 recommendations; there are some elements where you say, "countries that thought they had good guidance turned out that they didn't." We also recognized that there were significant numbers of treaties that were not fully in accordance with the minimum standard. The multilateral instrument is certainly a way that this is being addressed now.



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How can we minimize the instances of those adjustments that the competent authority itself doesn't actually think they should be defending and thus get chucked out of the process at that stage? That's something we want to explore in the MAP forum.

Beyond that, I think it's in the range we expected. The 24-month period (our targeted aspirational time line for a MAP case to be completed) is challenging, especially if you were to adjust the allocation and the non-allocation. You may look at the transfer pricing segment and say, "Twenty-four months – that is a real challenge for a number of administrations."

De Ruiters: Are there specific areas where you expect the most numbers and the most complex disputes to arise? And if so, what are those areas, and what can the OECD do to help prevent those disputes?

Pross: We're perhaps not there yet in the peer-review process. The team's extremely busy and settling in; we're seeing the first batches that are coming through the peer-review process. We are now setting up the new statistics, which will be published in November for the first time. This is actually very important, as it's the first time that we're going to compare apples with apples and oranges with oranges; we're going to have the same start date for all countries and the same end date.

Then the following year, we're going to have that data published jurisdiction by jurisdiction. So with that set of information, we get to the level of granularity where we can see whether there are particular typologies of cases that can be resolved as, for instance, how the US and India resolved particular types of cases under a structured program.

Now we're seeing some countries that have a lot of different MAP cases with a lot of other countries, and so that portfolio doesn't necessarily lend itself to a more structured solution, whereas with some of the others, we might be able to do it. We're also thinking that those resolutions found in MAP can then be brought either in forms of a safe-harbor type or other forms that help pre-empt some of these discussions and take the learnings and apply them to MAP proactively for the future.

De Ruiters: You implied that tax administrations' awareness of what's going on and what the new rules are, is very important to prevent disputes. Are tax administrations training their administrations well enough on the new rules, and does the OECD have a role in that?

Pross: I think they do. It's the beginning of many things, and of course we've seen activity in the past. Because of the peer review on MAP, people are more interested, engaged and eager to find ways of preventing things from going into the MAP pipeline. One of the ways to improve peer review is by simply having a smaller caseload.

Now, a smaller caseload can also come from limiting the sorts of adjustments that the field (i.e., field auditors) might make that the competent authority knows they won't be able to defend in a MAP.

How can we minimize the instances of those adjustments that the competent authority itself doesn't actually think they should be defending and thus get chucked out of the process at that stage? That's something we want to explore in the MAP forum. We have some global-awareness manuals, and there are some other ideas of how we can push back on the field so that those things don't happen.

We are also starting our training initiatives. A number of competent authorities have hired new staff in response to Action 14, as a result of the awareness that's been created around improving the MAP process, and so those people need to be trained.

The logical thing is to train these people together, to train them with their peers – not to train them in a single country to defend their individual assessments but rather train them with others to come to a principle-based resolution on the basis of the treaties that the countries have signed. So we bring them together, these new people as they come into the MAP function, and train them together by having mock-MAP negotiations, for example. That's what has started, and we want to build this up, and for once we also have some funding to be able to do that.

De Ruiters: One of the things that was advised in the MAP final report is that there could be better use of generally-applicable competent authority agreements, where on a technical issue you give guidance that the competent authorities take for future cases, and that guidance is published. Has the OECD or the FTA MAP forum already identified issues that they could work on in that respect? Is that something that the FTA MAP forum could take forward?

Pross: It's something that they could take forward, coordinating as necessary with Working Party 6, depending on what the nature is of that – but just because of the workload and other implications, we haven't done it yet.

Again, it's, as you said – too humbly, of course, because I think you developed it at the time – it's something where, as we move into the MAP forum, and we come to resolutions that we understand, how do we apply those prospectively so that we don't keep coming back to the same issues?

It is not that clear for those countries that have not historically had a principal purpose test how this is going to be applied in addition to existing rules that countries otherwise have, so there is uncertainty in the application.

For example, two countries have a cost-allocation case in MAP and we see how they resolved it. There is a principle underlying the resolution there – can we proactively then use some of that? That's certainly something we're trying to do. On the specific piece, which comes more in the Working Party 6 space, I probably need to reserve a little bit, because I can't really speak for that part of the house.

Action 6 and the Principal Purpose Test (PPT)

De Ruiter: Can you foresee a process whereby the interpretation of the principal purpose test (under BEPS Action 6) is taken forward in a coordinated fashion?

Pross: There was a good reason to do the Action 6, and that's now been translated into the principal purpose test, so that's where we are.

In terms of treaty shopping, we can see where we were, where we are no longer. So that's a good result, I think. That's what we intended to do. Now you have it, through the MLI, in approximately 1,100 treaties, so that's quite a lot. At the same time, you're absolutely right, in pointing out that now, and this is also what we hear from businesses – that there is uncertainty in the application. It is not that clear for those countries that have not historically had a principal purpose test how this is going to be applied in addition to existing rules that countries otherwise have. Now, it's new and it hasn't come in yet.

So there is a possibility of perhaps providing more guidance. We're probably not going to come to the place where every country will have the same exact understanding of the PPT; that's just the nature of sovereign countries and their court systems and how the administration of that will work.

Having said that, we are, at least at the OECD Secretariat here, exploring possibilities of simplifying life for certain collective investment structures, whether they're collective investment vehicles (CIV) or non-CIV, that are composed of taxpayers who themselves are entitled to treaty benefits.

So that's certainly a reflection that's currently ongoing. TRACE, because sits in that space; even this isn't what TRACE was designed for. It's certainly something that at the Secretariat level we're quite open to explore.



De Ruiter: The minimum standard has now clarified that if there is uncertainty or a dispute about whether or how the principal purpose test should be applied, it will get access to the mutual agreement procedure, correct?

Pross: Yes.

Action 7 and permanent establishment

De Ruiter: Another area of uncertainty is the permanent establishment area, and that, I think, has two dimensions. The first dimension is that the assessment of PEs is a factual matter, but there is currently already a lot of uncertainty about profit attribution to PEs, because there are no rules yet. That uncertainty seems to be exacerbated by the fact that there is a multilateral instrument where the new PE rules are being introduced, and some countries are adopting them, but others are not. Will there be any initiatives by the OECD to create more certainty in this area?

Pross: To understand the uptake of the PE provision, one can go to the MLI database and see where that stands. I believe that roughly 200 or 300 treaties so far will have it. The question, then, that you raise very legitimately is what is the profit attribution? There we have our paper, there's a consultation, we've had a lot of comments on the consultation document. The meeting of Working Party 6 is around the corner and the hope is that through the work of that group, we can come to better guidance and more clarity on the question of profit attribution to the PE in those circumstances.

Harmful tax practices

De Ruiter: Another minimum standard that your team is responsible for the peer reviewing is harmful tax practices. There are two elements to the kind of exercise – the exchange of rulings but also looking at existing regimes and assess

We've designed a box around a box, and we said "don't make it bigger than this," but this may sometimes be misunderstood; countries build exactly this, because this is what the international community accepts.

whether the kind of regimes that countries in the Inclusive Framework have are harmful or potentially harmful. Recently, a report on harmful tax practices was published, and it shows that the exercise is ongoing to assess these regimes. How many regimes were actually reviewed for this report?

Pross: A vast number. The total number, I think, is 164 regimes across the whole BEPS Inclusive Framework; so the OECD, the G20 countries, and those countries that subsequently joined the BEPS Inclusive Framework.

De Ruiter: What are the main conclusions or findings that came from the process?

Pross: I think we had a lot of focus in this work on patent boxes and IP regimes. That's not surprising, because IP is the big value driver, and we see this across the BEPS Action Plan, whether it's in transfer pricing and the correct taxation of IP, or whether it's in other areas, and we also see it in harmful tax practices.

Because IP is so significant, this is also where we see regimes where people try to attract IP. The key thing that we said in BEPS, as it relates to harmful tax practices and IP, is if you want to have a preferential regime on IP, then you are free to do so. There were some countries that would have liked to have no minimum taxation on mobile income, including intangible property. That's not where we ended up. But we did say that you need to only give benefits to income in proportion to that income being, if you wish, produced by the entity seeking to benefit from the regime. What does that mean? It means you need to undertake the value creation – essentially the R&D – and you're also entitled to reduced, beneficial taxation on the income in the proportion that you undertake the R&D.

So that was the principle, and then there were details, and the time lines, and how you had to change your regime, because nobody had a regime that was fully compliant with this, because it was an agreement that was reached at the OECD in this process.

And so if we now look out, in Europe, but also far beyond, we essentially have practically every single IP regime either amended to conform to the international standard, or abolished, or in the process of being abolished. I think this is challenging for new countries that have just joined, and are being told they need to change their IP regime and amend their legislation. So effectively, everybody has 12 to 15 months to make those changes, and they're now being counted as in the process of being abolished if they committed at the government level to their peers, that they will make the change. So you see tremendous change in IP regimes, where basically the whole world is now consistent

with the standard, with the exception of France, which is the one country that has not yet amended its IP regime.

So that's the story on IP. I think it's a tremendous success story of seeing so much consistency, something that business always argues for, and that we have achieved here. Importantly, we're not recommending to even have the patent box. But what the principle says, if you are having a box, then "don't make it bigger than this."

So in some sense, it's a box around a box, and one that we see implemented across the world, with one exception. On the non-IP regimes, whether they're leasing, financing, shipping, etc., I think what we're seeing is a tremendous move to remove ring-fencing, this was still an issue outside Europe, perhaps outside the traditional OECD countries, where this was something maybe even in the design of regimes that was done 10 years ago, but we still find it in other countries, and that's being removed across the board.

And we're also seeing that – again, consistent with the value creation – that there are changes being made to assure that every preferential regime requires substantial activities to take place in the regime, and only then is it an acceptable regime. So across the 103 BEPS Inclusive Framework members [Editor's note: now 111] you see tremendous change: things that have already happened, and things that are in process; we now need to make sure that it actually happens, to the extent that we have a commitment, and so we have a monitoring, follow-up process that will keep us busy certainly over the next 12 to 15 months.

De Ruiter: The OECD has said on many occasions that IP and patent boxes are bad tax policy. But – perhaps because the standard is clear – we see countries introducing these boxes. So with that, the OECD criteria has become a target to meet by a country, and I'm not sure that was the intention of the OECD. So if countries would like to stimulate research and development activities, what would you advise them in relation to IP boxes or other incentives?

Pross: You're absolutely right, and I appreciate the question. As I said, we've designed a box around a box, and we said "don't make it bigger than this," but this may sometimes be misunderstood; countries build exactly this, because this is what the international community accepts. Of course, just because it's not harmful doesn't make it into good tax policy. There seems to be clear indications that to encourage R&D, picking up on the expenses – front-loading rather than back-loading – seems to be a more effective way to get to better results, whether this is double deductions, whatever this might be. And also, to be clear, there isn't anything in the BEPS space that should or would stop countries from incentivizing R&D activities taking place. That part of tax policy design has nothing to do with BEPS and needs to be decided by the countries as they design their tax policies.



Pascal Saint-Amans – Director of the OECD's Centre for Tax Policy and Administration

Remarks at EY's International Tax Conference, 5 October 2017, New York

Pascal Saint-Amans, Director of the OECD's Centre for Tax Policy and Administration, addressed clients and EY tax professionals this month at the opening of EY's 2017 International Tax Conference.

There were many areas of interest within Saint-Amans' remarks, including that:

- ▶ *"A big thing which has not been dealt with adequately by the BEPS project is the digital economy".*
- ▶ *"We, at the OECD, strongly disapprove of unilateral measures. But it's going to be hard to tell countries not to move, if there is no prospect of any form of agreement. That's where we turn to the US, and hope that the US will send messages that there is the possibility of an agreement of new rules being developed in the next couple of years."*
- ▶ *"Maybe the highest source of uncertainty in today's environment is US tax reform" and that "You (the US) have to move to a territorial system, like all the other countries... ..if you want to grow your competitors, your champions, your multinational companies, in a way that allow them to grow abroad and then to repatriate their profits, to create employment in this country, you must move to a territorial system."*
- ▶ *"We would like to go even further than the minimum standards, and ensure that on transfer pricing, for instance, we are able to understand who is doing what at the national level."*





BEPS

The OECD's Multilateral Instrument (MLI): spotting trends among the data

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Put in perspective, BEPS has been in our jargon for much of the present decade, and an unprecedented number of countries have committed to systematically, coherently and consistently implement the BEPS minimum standards. To facilitate and expedite this, new approaches were considered, the end result being an entire Action of the BEPS Action Plan, Action 15.

The objective of Action 15 was to analyze the tax and public international law issues related to the development of a multilateral instrument that would enable jurisdictions to implement, through the signing and ratification of the instrument, the treaty-based measures developed in the

course of the BEPS project. On the basis of this analysis, it was concluded that such an instrument was not only feasible but desirable and, under a G20 mandate, an ad hoc group was created to negotiate the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS (also known as the MLI), which was agreed upon in November 2016. The MLI has been open for countries to sign since 1 January 2017.

MLI signatories

To date, 71 jurisdictions have signed the MLI and 7 have expressed their intent to sign in the near future¹. The MLI is open for signature by virtually any jurisdiction, irrespective of whether the jurisdiction is an OECD member or a member of the Inclusive Framework (IF) on BEPS. In fact, from the 78 jurisdictions that have either signed or expressed their intent to sign, 7 are not members of the IF on BEPS. This can be seen as a signal that these non-BEPS member jurisdictions may be considering becoming BEPS members, which in turn would imply that more jurisdictions will be implementing the BEPS minimum standards in the future.

The IF on BEPS is currently comprised of 111 members. Sixty-six members have signed the MLI, and five have expressed their intent to sign it. Pascal Saint-Amans, the Director of the OECD's Center for Tax Policy and Administration, recently told the audience at EY's International Tax Conference² that "we have another 30 (jurisdictions) in the pipeline. So by mid-2018, the MLI will cover around 100 jurisdictions." This is an unprecedented achievement in the international tax arena. For international tax, MLI represents the most subscribed-to instrument ever. In comparison, the original Convention on Mutual Administrative Assistance in Tax Matters (MAAC) has been open to the signature of member states of the Council of Europe and OECD since 1988. As of 1989, these international organizations had 21 and 24 members respectively.

Likewise, the amending protocol to the MAAC was also open for signature by members of the Council of Europe and OECD countries, and to any other jurisdiction that requests to be invited to sign the MAAC and its amending protocol. During the first signing of the amended MAAC, just 15 jurisdictions signed the MAAC and/or its amending protocol.

In light of these examples, it is not only clear that the MLI is a milestone, but also that the MLI is evidence of the shift toward a more multilateral mindset in international taxation.

Countries' MLI positions

Minimum standards

Once a jurisdiction signs the MLI, it must submit a (preliminary) list of tax treaties that it would like to be covered. When a tax treaty in force is included in both parties' lists, the tax treaty becomes a Covered Tax Agreement (CTA).

A signatory must also submit a list of positions reflecting the changes they would like to make to its CTAs. Generally, when both parties to a Covered Tax Agreement (CTA) have matching positions MLI provisions, those provisions will apply to that CTA - with the exception of provisions allowing for asymmetrical application. In early 2017, the OECD held multi-country negotiations sessions, to help countries establish their initial positions.

From analyzing the preliminary positions of the MLI signatories to date, it is clear that the MLI provision with the broadest application is the Principal Purpose Test (PPT) contained in Article 7 of the MLI. All 71 signatories have chosen to adopt a PPT, 12 have chosen to apply a Simplified Limitation on Benefits (S-LOB) rule in addition³, and 9⁴ have included a statement indicating that they intend, where possible, to adopt a detailed LOB, in addition to or in replacement of a PPT.

1. Armenia, Cyprus, Fiji, Kuwait and Serbia have signed the MLI, and Tunisia and Lebanon have expressed their intent to sign the MLI.

2. See full remarks at: <http://www.ey.com/gl/en/services/tax/tax-policy-and-controversy/remarks-of-pascal-saint-amans-at-ey-2017-international-tax-conference>

3. Argentina, Armenia, Bulgaria, Chile, Colombia, India, Indonesia, Mexico, Russia, Senegal, Slovakia, and Uruguay

Jurisdictions are clearly concerned about tax avoidance and want to quickly access new tools (e.g., a PPT) to tackle the issue. At the same time, they are aware of the increasing number of tax disputes and the need for more effective dispute resolution. It seems, however, that is not a pressing issue for a number of jurisdictions that would rather comply with the minimum standard in BEPS Action 14 (*Making Dispute Resolution Mechanisms More Effective*) outside the MLI.

Only Mauritius indicated that it intends to negotiate a detailed LOB in replacement of the PPT, and only Chile indicated that it intends to negotiate a detailed LOB in addition to the PPT. The remaining seven jurisdictions will pursue either a detailed LOB in addition to or in replacement of a PPT.

The above is not surprising, given that the minimum standard in Action 6 (*Preventing the Granting of Treaty Benefits Inappropriate Circumstances*) requires all BEPS members to have a minimum level of protection in their tax treaties against treaty shopping and tax avoidance.

Although jurisdictions can choose to meet these minimum standard via bilateral negotiations, none made this choice - not even signatories who are not BEPS members, and thus are not committed to this minimum level of protection.

In contrast, 24 jurisdictions made a reservation to not apply Article 16(1) (Dispute Resolution) on the basis that they intend to meet the minimum standard for improving dispute resolution outside of the MLI.

It is interesting to put these two MLI articles in perspective: Jurisdictions are clearly concerned about tax avoidance and want to quickly access new tools (e.g., a PPT) to tackle the issue.

At the same time, they are aware of the increasing number of tax disputes and the need for more effective dispute resolution. It seems, however, that is not considered a treaty issue for a number of jurisdictions that would rather comply with the minimum standard in BEPS Action 14 (*Making Dispute Resolution Mechanisms More Effective*) outside the MLI.

Given that the PPT will probably be the MLI provision applied the most (as well as, ironically, potentially driving the largest number of future disputes!) it would be beneficial if the OECD were able to provide additional guidance on its application. This in turn may also help reduce disputes.

Furthermore, jurisdictions' experience administering and applying these kind of rules is somewhat unclear. The MLI has a specific reservation that jurisdictions can make for the PPT to not apply to a CTA which already has a PPT. Using this reservation as a point of reference, an estimate can be made of how many CTAs have an equivalent PPT, and also which countries may have prior experience in applying a PPT.

Surprisingly, just 11 jurisdictions (i.e., 15% of the signatories) made this reservation, and, in total, 38 tax treaties were listed as having a provision within the scope of this reservation.

This is a relatively low number, considering that there are cases in which, although both contracting jurisdictions made this reservation, their specific CTA is not listed as having a provision within the scope of the reservation. For example, Chile listed the CTA with Italy as being within the scope of this reservation, while Italy did not list their CTA with Chile as being within the scope of the reservation by either or both of the signatories.

Also, some jurisdictions did not make this reservation in spite of already having a PPT provision in a CTA. For example, China did not make this reservation and Chile and Germany listed their CTA with China as being within the scope of the reservation.

But overall the message is clear: few jurisdictions have much PPT experience.

Optional provisions

In terms of optional provisions (i.e., those that are not BEPS minimum standards), the provisions that seemed less desirable to jurisdictions are the anti-abuse rules for PEs situated in third jurisdictions (Article 10 of the MLI) and the saving clause that clarifies that the treaty does not restrict a jurisdiction's right to tax its own residents, except with respect to certain treaty provisions (Article 11 of the MLI).

Forty-nine jurisdictions (i.e., 69% of the signatories) made a reservation for Article 10 and 11 of the MLI not to apply to their CTAs.

Conversely, the most attractive provision is Article 13 of the MLI which deals with the artificial avoidance of PE status through the specific activity exemptions provision.

Article 13 contains two substantive provisions. On the one hand, Article 13(1) contains a set of options on the interpretation of the list of specific activity exemptions. On the other hand, Article 13(4) contains an anti-fragmentation clause. 44 signatories (i.e., 62% of the signatories) indicated that they would like article 13(1) to apply, by not making a reservation. For the purpose of Article 13(1), signatories were required to choose whether they wanted:

- ▶ Option A (i.e., each of the exceptions included in that provision needs to meet the "preparatory or auxiliary" threshold)
- ▶ Option B (i.e., each of the exceptions is intrinsically preparatory or auxiliary and, thus these activities should not be subject to the "preparatory or auxiliary" threshold) or;
- ▶ None of the options.

Jurisdictions may still change their positions on what to include in the MLI: This may occur until their ratification of the MLI. And even after that, they can add additional measures, but this would require a new ratification process.

The preference of jurisdictions towards option A is clear. From the 44 signatories that want to apply this MLI provision, 77% of the signatories want option A, 16% option B and the remaining 7% did not choose an option.

With respect to the anti-fragmentation clause, from the 44 signatories that wish to apply Article 13, only four jurisdictions (Austria, Germany, Luxembourg and Singapore) reserved the right for the anti-fragmentation clause not to apply, i.e., 91% of the signatories wishing to apply Article 13 of the MLI, also want the anti-fragmentation clause.

European dimensions

Surprisingly, a significant number of jurisdictions not wanting to adopt the PE provisions are European Union (EU) Member States (MS). This is surprising in light of the European Commission (EC) recommendation on the implementation of measures against tax treaty abuse wherein Member States were encouraged to implement and make use of the new PE provisions in order to address artificial avoidance of PE status as drawn up in the final report on Action 7.

Overall, 40 jurisdictions (i.e., 56% of the signatories) do not want to apply the broadened agency PE definition (Article 12 of the MLI). At the EU level, where 27 out of 28 MS have signed, 19 EU jurisdictions (i.e., 70% of EU MS signatories) do not want to apply the broadened agency PE definition.

The EC also encouraged Member States to include a PPT in the tax treaties that they conclude among themselves or with third countries. The recommended PPT, however, has additional language over and above the PPT in the MLI. The additional European language, which aims to align the MLI PPT with EU law, provides that treaty benefits cannot be denied under the PPT in cases of a genuine economic activity.

This additional language could have easily been included in the MLI as an option, enabling EU MS to follow the EC recommendation. It is unclear why this did not occur, particularly since the final report on Action 6 acknowledges that "Some countries may have constitutional restrictions or concerns based on EU law that prevent them from adopting the exact wording of the model provisions that are recommended in this report For these reasons, a number of the model provisions included in this report offer alternatives and a certain degree of flexibility."

Moreover, it comes as a surprise that the OECD has not included this additional language in the MLI PPT, considering that the EU is a G20 member.

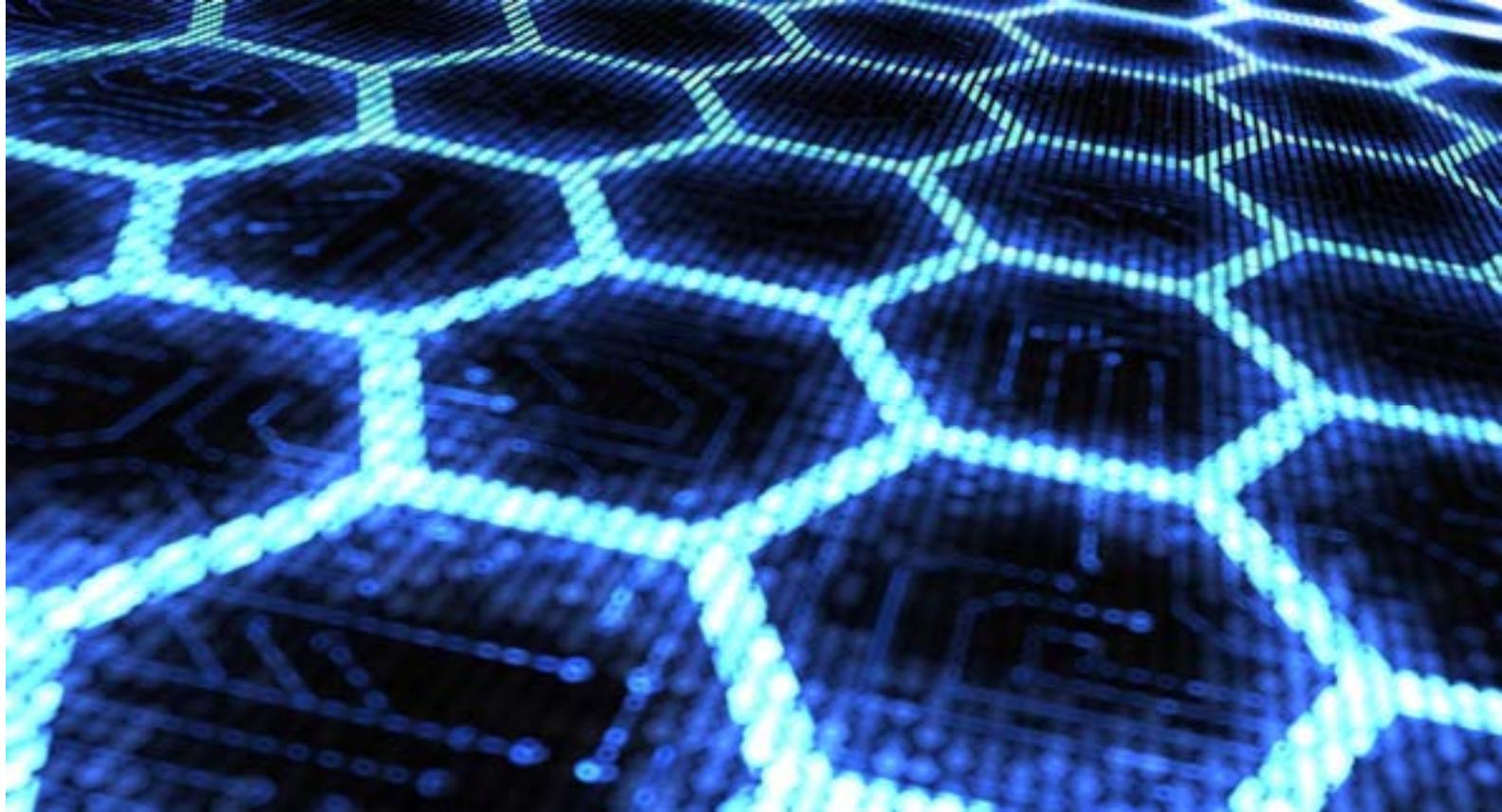
Moreover, all EU Member States participated in the work on BEPS, and that the OECD took into account the particularities of EU law (see for example final report on Action 3 on designing effective Controlled Foreign Company (CFC) rules).

The way forward

As we move through 2018, a number of factors become clear:

- ▶ Jurisdictions may still change their positions on what to include in the MLI: this may occur until their ratification of the MLI. And even after that, they can add additional measures, but this would require a new ratification process.
- ▶ There will be a second signing ceremony: This will likely occur around the fourth plenary meeting of the Inclusive Framework on BEPS (expected in January 2018). From the IF on BEPS, only the US is not likely to sign the MLI. This leaves 31 other BEPS members that may be considering signing the MLI in the second signing ceremony (in addition to any non-BEPS members).
- ▶ The MLI will come into effect in 2018: This will happen on the first day of the month following the expiration of a period of three calendar months beginning on the date of deposit of the fifth instrument of ratification, acceptance or approval. So far, Austria and the Isle of Man have submitted their ratification instruments and confirmed their positions without making any changes. Singapore and Poland will likely be next in line.
- ▶ Implementation of the treaty-based BEPS recommendations through bilateral negotiations will continue: Some jurisdictions had been renegotiating and concluding new tax treaties containing BEPS recommendations before the BEPS final reports were released. However, it seems this has not attracted much attention, yet there are treaties coming into force which already contain the new PE definitions, a PPT and/or other treaty-based BEPS recommendations. It is important to monitor these treaties; they can give us hints and lessons on how certain MLI provisions will be applied/construed in practice by some jurisdictions.
- ▶ The 2020 BEPS review may drive new MLI articles: It is important to keep in mind that the IF on BEPS will undertake a BEPS review in 2020. Depending on the outcomes of this review, we may see new BEPS recommendations agreed as minimum standards. In turn, new treaty-based recommendations could lead to jurisdictions agreeing to withdraw certain reservations that become minimum standards.

Although the future remains unclear, it is certainly a moment of continuous change. Given the amount and speed of changes, one cannot wait for the dust to settle down to take action. It is critical to adapt and anticipate in the current times.



Digital tax policy disruption

Widespread unilateral moves probable if consensus cannot be achieved

Reignition: In early October, Pascal Saint-Amans, Director of the Centre for Tax Policy and Administration at the Organisation for Economic Co-operation and Development (OECD), addressed EY clients and professionals at EY's International Tax Conference in New York, saying¹, *"A big thing which has not been dealt with adequately by the BEPS project is the digital economy."*

Would those words have been included if we had not seen such vigorous debate and activity on digital taxation in Europe in the last few months? Perhaps not.

At the heart of the matter is a growing sentiment in Europe – to which not all EU Member States subscribe – that the consensus position developed within BEPS Action 1 that there is "no such a thing as a separate digital economy, but that companies are now participating in the digitalized economy" is not sustainable, and that action needs to occur sooner, not later. And the European Commission is certainly acting quickly, detailing a number of both short- and long-term proposals, in turn increasing the pressure on the OECD to move more quickly.



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1. "Remarks of Pascal Saint-Amans at EY's 2017 International Tax Conference," EY website,

Indeed, at a November 2017 public consultation, Saint-Amans noted, “There were four key findings in the Action 1 work; the first was that the title was probably wrong – it was not tax and the digital economy but the tax consequences of the digitalization of the economy.”

The sentiment change appears based on the belief that OECD Base Erosion and Profit Shifting (BEPS) Actions 2-15 may not be effective at addressing the tax challenges posed by businesses that have a very low physical presence (being intellectual property (IP) and/or data-intensive companies, including those transacting solely on internet platforms).

Therein lies a big piece of the problem – this issue does not necessarily seem to be about taxing the digital economy as a whole as much as it is about taxing a small subset of digital activity. Indeed, at the OECD’s November 2017 public meeting² in Berkeley, California, Saint-Amans clearly communicated that that specific aspect was high on the mind of the OECD. He referred to ongoing work as instead addressing the “tax challenges of digitalization” and not focussing on a particular set of companies, demonstrating the OECD’s intimate grasp of the arguments put forth by the Commission.

Indeed, at the November 2017 public consultation, Saint-Amans noted, “There were four key findings in the Action 1 work; the first was that the title was probably wrong – it was not tax and the digital economy but the tax consequences of the digitalization of the economy.”

Notwithstanding those viewpoints, some EU Member States in particular have grown increasingly impatient at the perceived lack of progress being made by the OECD (with an interim report on Action 1 due in spring 2018, followed by a final report, which the OECD said at a recent event could be bought forward from 2020 to 2019), and are keen to make sure that, by the end of spring 2018, there is a concrete answer on how to move forward. This is in turn encouraging the Commission to act, driving a whole new raft of activity in September, October, and November 2017.

The vigor of the Commission in pursuing its goals should not be underestimated. Indeed, in its own words, the Commission says³ that (EY bolds for emphasis):

- ▶ “Unfortunately, it has so far proved difficult to agree on the solutions at global level, as is evident from the OECD report in October 2015. The time to act has now come.
- ▶ An important milestone will come early in 2018 when the OECD will present an interim report on the taxation of the digital economy to the G20. It is essential that this report comes to appropriate and realistic conclusions on the way ahead and identifies genuine policy options to tackle the challenge.

- ▶ In parallel, the EU must examine all possible options so as to adopt new rules for taxing the digital economy within the Single Market. It should also focus on EU solutions if progress at international level proves too slow.
- ▶ The EU expects a high level of ambition as regards the interim report on the taxation of the digital economy that the OECD will present to the G20. It is essential that the report comes forward with meaningful policy options to address the issues at stake.
- ▶ Only a coordinated EU approach will ensure that the solution is fit for the Digital Single Market.
- ▶ In the absence of adequate global progress, EU solutions should be advanced within the Single Market and the Commission stands ready to present the appropriate legislative proposals.”

Moreover, in the same publication the Commission notes “a comprehensive and modern approach to the taxation of the digital economy is needed to meet the goal of fairer and more efficient taxation, and to support EU growth and competitiveness through the Digital Single Market.”

“The objective of the Presidency,” said a mid-October 2017 Presidency paper,⁴ – “is to have these conclusions adopted at the ECOFIN Council meeting of 5 December 2017, for input into parallel OECD discussions on their interim report to be delivered at the G20 Finance Ministers meeting of April 2018 and for the Commission in preparing the possible legislative proposal in Spring 2018.” While that adoption did occur at ECOFIN, the overall outcome was not quite as clear-cut; as this article will discuss, a series of further steps to test the legal basis and overall financial impacts of the conclusions was also agreed.

The current debate focuses almost exclusively on the taxation of businesses located in source countries, and not the taxation of individuals receiving such goods or services in countries of residence. That latter issue was addressed by the OECD in BEPS Action 1, with the OECD calling for countries to “apply the principles of the OECD’s International Value Added Tax and Goods and Services Tax (VAT/GST) Guidelines as well as consider the introduction of the collection mechanisms included therein” – a call clearly heeded by many countries, as digitally focused new Value-Added and Goods and Service taxes were some of the most commonly-introduced indirect taxes around the world in 2016⁵.

2. “BEPS public consultation on the tax challenges of digitalisation,” *OECD website*, <http://www.oecd.org/tax/beps/public-consultation-on-tax-challenges-of-digitalisation-1-november-2017.htm>, 1 November 2017.

3. “Communication from the Commission to the European Parliament and the Council: A Fair and Efficient Tax System in the European Union for the Digital Single Market,” https://ec.europa.eu/taxation_customs/sites/taxation/files/1_en_act_part1_v10_en.pdf, 21 September 2017.

4. “Challenges of the digital economy for direct taxation – State of play and the way forward,” ECOFIN meeting document, <http://www.politico.eu/wp-content/uploads/2017/10/Digital-tax.pdf>, 11 October 2017.

5. “Digital tax developments map,” *EY website*, http://www.ey.com/gl/en/services/tax/ey-digital-tax-development-map?utm_source=ey-digital-tax, June 2017.

Overall, pressure is dramatically increasing on the OECD (and by logical extension, the United States as co-chair of the Task Force on the Digital Economy, the body in the OECD addressing this issue) to develop its recommendations earlier, and in more final form.

The Commission has therefore drawn up a series of suggestions and proposals, which are now being assessed with a view to presenting such a go-forward legislative plan. The Commission's suggestions for assessment – as they currently stand – are split between short- and long-term tax measures (by which it means more sustainable policies). Most recently, the Commission opened a public consultation on the issue. That public consultation closed on 3 January 2018, i.e., around a month after proposals were first put forward. That is a puzzling approach to taking public input.

Depending on the pace of progress toward an agreeable (to the Commission) long-term solution by the OECD, it is possible that any short-term European proposal may potentially fall by the wayside prior to implementation, with Member States and the Commission instead putting their support behind a longer-term solution.

Overall, pressure is dramatically increasing on the OECD (and by logical extension, the United States as co-chair of the Task Force on the Digital Economy (TFDE), the body in the OECD addressing this issue) to develop its recommendations earlier, and in more final form.

The OECD has already requested public input regarding the challenges and potential solutions to digital taxation. The input was requested by 15 October, reviewed by the TFDE on 23 October and published⁶ on 25 October 2017. The OECD also held a public consultation on the US West Coast in early November.

EY provided input⁷ to the OECD request, noting, among other things that:

“EY would first like to express its concern about the current environment, where individual countries and potentially the European Union are moving in a direction that has led, or may lead, to taxation that may conflict with long established international principles, such as the principles embodied in more than 3,000 existing bilateral tax treaties.

“These principles are designed to prevent double taxation and provide for a neutral platform on which companies can perform their critical business activities without being discriminated against, or favored, based on residence, industry sector, or forms of commerce.

“Furthermore, these principles, which have evolved over several decades, have contributed greatly to worldwide economic growth. A departure from these principles in a non-coordinated fashion is not conducive to the prevention of double taxation and, therefore, to sustained economic growth.”

And that:

“As pointed out within the Action 1 Final BEPS Report, the digital economy is the overall economy. The digital economy cannot be ring fenced or separately distinguished.”

If any OECD recommendation(s) is deemed to be aligned to the Commission's objectives, then coherence between the organizations may actually increase, and they may well move forward on a common agenda; if the OECD does not deliver concrete recommendations to a suitable timetable, or if such recommendations are not aligned to the Commission's wishes, there is a significant risk that the Commission will push forward unilaterally with their proposals. If the OECD says that one of the options (see below) being studied by the Commission is one of several options of interest to OECD member countries, this would be seen as providing the Commission with a (very) implicit “green light” under which they will proceed.

In particular, the Commission is believed to be looking at multiple goals in regard to the digital tax debate alongside the stated goals of fairness, competitiveness, integrity of the single market and sustainability. These goals include using the debate as a way to generate momentum for the Common Consolidated Corporate Tax Base (CCCTB) project.

6. <http://www.oecd.org/tax/beps/public-comments-received-on-the-tax-challenges-of-digitalisation.htm>, 25 October 2017.

7. “Tax Challenges of Digitalisation,” *OECD website*, <http://www.oecd.org/tax/beps/tax-challenges-digitalisation-part-1-comments-on-request-for-input-2017.pdf>, 25 October 2017.

Unilateral developments continue to play out

While the re-ignition of the debate on the taxation of digital activity certainly seems to be increasing in volume, as this publication was released, a number of individual countries either addressing or impacting digital taxation were playing out:

- ▶ In Italy, The Italian 2018 Budget Law introduced a new “Tax on digital transactions”⁸ (referred to locally as the “Web Tax”) with significant amendments compared to the initial draft law¹ (the Draft), and a new definition of permanent establishment partially in line with the OECD’s BEPS Action 7. According to the final version of the Law, the Web Tax is:

- ▶ Levied at a 3% rate on the value of each digital transaction
- ▶ Due by resident and nonresident enterprises concluding more than 3,000 digital business to business transactions in a calendar year and will not be creditable from the Italian income tax
- ▶ Settled by the buyers of the services

The PE investigation for significant nonresident digital suppliers included in the Draft has been removed from the final version of the Law.

- ▶ In the United Kingdom, the government opened a consultation on 1 December 2017 on the design of rules expanding the circumstances in which a royalty payment to persons not resident in the UK gives rise to a liability to income tax. The intention is that any royalty payment made in connection with UK sales to a low or no tax jurisdiction will be subject to tax, even if the group has no taxable UK presence under current rules. The government notes that it will respect the international obligations in the UK’s tax treaties in the application of the measure. This punitive and extraterritorial withholding tax charge will potentially create further pressure for impacted companies to onshore their intellectual property, but also provides such companies with a period of time to evaluate how the dust settles around US tax reform. The changes will have effect from April 2019. Alongside the consultation, the UK government also published a position paper titled *Corporate tax and the digital economy*⁹. In summary, the paper seeks to define the problem narrowly, addressing not the taxation of all digital activities, but rather focusing its lens on the smaller set of companies that fit the “IP and/or data intensive” description offered at the start of this article. Furthermore, it stresses the need for both multilateral agreement and a delayed date for any action. At a more detailed level, the paper reaffirms and defends the arm’s-length principle for most technology sector issues and most companies.

Overall, one could argue that the UK paper may drive the ongoing debate in one of two ways. On one hand, it may actually have the effect of implicitly putting some boundaries on one element of the EU’s desire – being to differentially focus efforts on “platform” companies that may resell user activity back to the state of residence of such users. On the other, it could equally be argued that the UK government is giving an implicit green light to further unilateral action, including by the EU.

Other countries, too, are known to share similar eagerness to try and capture additional tax revenues as those above. This includes large developing markets such as Brazil and China, each of which may well press ahead with their own unilateral actions should a consensus position not emerge in the next few months.

Brazil is believed to be an advocate for revised digital nexus concepts, while China is perhaps at an earlier stage in the decision-making process, continuing to assess OECD developments (where China is part of the BEPS Inclusive Framework) while also openly facilitating discussion about any potential sovereign approach.

7. “Italy considers Web Tax and other measures for digital economy,” EY Global Tax Alert, <http://www.ey.com/gl/en/services/tax/international-tax/alert-italy-considers-web-tax-and-other-measures-for-digital-economy>, 4 December 2017.

8. “UK 2017 Autumn Budget: Key business tax announcements,” EY Global Tax Alert, <http://www.ey.com/gl/en/services/tax/international-tax/alert-uk-2017-autumn-budget-key-business-tax-announcements>, 22 November 2017.

9. “Corporate tax and the digital economy: position paper,” GOV.UK website, <https://www.gov.uk/government/consultations/corporate-tax-and-the-digital-economy-position-paper>, 22 November 2017.

The Presidency also sees the possibility of a new nexus definition, which would work within the current corporate income tax system, but which introduces changes to ensure the rules work with the digital presence.

The EU's political position

The European Council, made up of the heads of state of the 28 EU Member States, included a discussion of the tax challenges of the digital economy as part of its summit in Brussels held on 19-20 October 2017. This follows on from the EU's Working Party on Tax Questions considering the leaked paper referred to above in its meeting on 16 October.

The European Council discussions follow on from the informal meeting of the Economic and Financial Affairs Council (ECOFIN)¹⁰, made up of the finance ministers of the Member States, in Tallinn, Estonia, in September. A few days prior to this meeting, the Finance Ministers of four Member States (France, Germany, Italy and Spain) called, in a letter, for the EU to introduce measures to tackle the tax challenges posed by the digital economy, which could include an equalization levy, as reaching a global consensus via the OECD's work was perceived as progressing too slowly.

Following the ECOFIN meeting, a number of other Member States showed public support for the proposals, and French Prime Minister Emmanuel Macron said in a speech that 19 Member States were in support. The discussions at the European Council summit on 19 October 2017, however, demonstrated that there remain deep divisions among EU Member States.

It is reported that the European Council engaged in a fierce debate over the digital tax proposals, with Ireland and Luxembourg both cautioning against the EU acting independently of the global work being undertaken by the OECD. Leo Varadkar, the Irish Prime Minister, shared his views that any digital tax proposal should be considered from a global perspective, a stance which is understood to be backed by several other Member States. In recognition of these views, the conclusions adopted by the European Council note that, in relation to an effective and fair taxation system fit for the digital era, "it is important to ensure that all companies pay their fair share of taxes and to ensure a global level-playing field in line with the work currently underway at the OECD."

While the European Council conclusions invite the European Commission to pursue its examination of the options for addressing the tax challenges, as set out in the Commission's post-ECOFIN paper published on 21 September 2017¹¹ (and further analyzed in the leaked paper), and to present these options by early 2018, the discussions demonstrate that the unanimous support required for tax measures to be introduced into the EU may still be some way off in this matter. That presents a challenge; while the enhanced cooperation route remains an open possibility, the Commission will not want to deliver an outcome that is only supported by a subset of Member States, as it would not want to be seen driving new measures that attract anything less than full consensus.

The European Commission's proposals

A stalking horse for the CCCTB?

The Working Party on Tax Questions has also discussed the topic of digital tax as part of its work on the proposals for a CCCTB, and the Working Party meeting held on 16 October 2017 was scheduled to start with an overview of the challenges of the digital economy for direct taxation (with an exchange of views on the way forward), before moving on to continue the article-by-article review of the proposed directive for a CCCTB.

The Presidency report that the working party used as a basis for their discussions sets out two main options to tax the digital economy (one short term and one long term), being an equalization levy or a new tax nexus.

Equalization levy

A new equalization levy is seen by the Commission as a straightforward option as it operates outside existing double tax treaties (and so would not violate them), but, as it will be a new tax, agreement would be needed on the tax base, rate and who it should target.

The levy, the Commission say, *could* be designed to have a narrow (e.g., fees from advertising only) or more comprehensive scope (e.g., digital services provided in the market country), although it will also be necessary to consider compatibility with other international agreements (e.g., the World Trade Organisation agreements) if it is to be applied to revenues earned by non-EU residents.

10. "ECOFIN discusses development of new digital taxation rules," EY Global Tax Alert, <http://www.ey.com/gl/en/services/tax/international-tax/alert--ecofin-discusses-development-of-new-digital-taxation-rules>, 19 September 2017.

11. "Communication from the Commission to the European Parliament and the Council: A Fair and Efficient Tax System in the European Union for the Digital Single Market," https://ec.europa.eu/taxation_customs/sites/taxation/files/1_en_act_part1_v10_en.pdf, 21 September 2017.

The trends of digitization are pervasive in companies within all industry sectors, and the business models we see today are likely to see wide-spread adoption in various forms in nearly all global enterprises. This means that special measures may inconsistently and haphazardly become generally applicable rules.

In the paper, the Presidency emphasizes that this option should be a temporary one, since it considers it would be difficult to apply to “B2C” business models supplying directly to consumers and because it will not tax value where it is created, since the tax base could not be profits, which is one of the primary objectives the Commission is trying to achieve. Of course, the core issue of digital is a tough enough nut to crack on its own; other macro challenges – Brexit, potential policy responses to US tax reform and how to address supply chains that include non-EU segments must also be addressed. Likewise, more granular issues such as agreeing on the rate, base and level of obligation of Member States to adopt an exact measure also remain.

The paper includes a summary of the Indian equalization levy, as well as an overview of the French vision for the EU equalization levy, to give examples as to how such a regime may operate.

A digital nexus definition

The Presidency also sees the possibility of a new nexus definition, which would work within the current corporate income tax system, while introducing changes to ensure the rules work with the digital presence. In the view of the Presidency, this would ensure that international dispute resolution mechanisms could continue to apply, unlike for an equalization levy.

There are a number of ways a new nexus could be implemented, but the Presidency sees three options – all of which would need to consider some form of amendment to existing transfer pricing and profit apportionment methodologies, thus potentially interfering with international taxation norms – as being most promising:

- ▶ Amendments to bilateral treaties between Member States through a coordinated protocol, which would allow for action within Europe, but may create discrepancies with third countries.
- ▶ Amendments to the existing Anti-Tax Avoidance Directive (ATAD), which would provide a consistent implementation within the EU, but could override treaties with third countries and so lead to disputes. Effectively, such a development would represent “ATAD III.”
- ▶ Introducing a new apportionment rule into the Common Consolidated Corporate Tax Base (CCCTB) proposals, although it is recognized that this would be impossible to apply to third countries and also that obtaining consensus within the EU in the short term on a CCCTB may prove difficult.

The paper also considers the pros and cons of the EU acting without global agreement, noting that while being proactive can speed up the implementation and avoid piecemeal, unilateral measures by EU Member States, it could impact EU competitiveness and create double taxation disputes with non-EU countries – a point reinforced in EY’s submission into the OECD’s request for input.

The Estonian Presidency presented draft conclusions to the High Level Working Party on Tax Questions on 27 October 2017, ready for these to be adopted at the ECOFIN Council meeting on 5 December, where the Presidency is looking to reach consensus amongst the Member States on the way forward.

Latest from the EU

On 5 December, ECOFIN – the EU body within which government economy and finance ministers from each EU Member State meet to discuss, amend and adopt laws, and coordinate policies – published their conclusions¹² titled “Responding to the challenges of taxation of profits of the digital economy.” The Council conclusions show that overall support on the proposed solutions (short- and long-term) was secured. Indeed, this fact alone is significant. While the conclusions may represent a slight slowing in the pace of developments in this area, they do not represent a significant change in direction for the EU.

Clause 25 of the conclusions in particular provides insight into potential future direction, noting that the Council “looks forward to appropriate Commission proposals by early 2018, taking into account relevant developments in ongoing OECD work and following an assessment of the legal and technical feasibility as well as economic impact of the possible responses to the challenges of taxation of profits of the digital economy.”

The reference to legal and technical feasibility as well as overall economic impact illustrate that the Council – and by logical extension, the Commission – want to do everything they can to continue to ready their proposals, allowing them to both influence the OECD’s April 2018 report on the taxation of digitalized business for the G20 leaders, and also to move quickly once the OECD report is published, should its findings not meet with their approval.

12. “Council conclusions on ‘Responding to the challenges of taxation of profits of the digital economy,’” Council of the European Union, <http://www.consilium.europa.eu/media/31933/st15175en17.pdf>, 30 November 2017.

Whatever outcomes emerge, any new ways of taxing “digital activity” will of course bring design and implementation challenges, as the Commission paper itself acknowledges.

Where does all this leave the OECD?

The most recent indications of future OECD direction came from a US West Coast public consultation¹³ in early November.

There were a very small number of US-based/Silicon Valley companies present and mostly European policy advocates along with the full Task Force on the Digital Economy (TFDE) and OECD leadership teams. It was a very open and positive discussion, but clearly highlighted the challenges in front of the OECD. These challenges seemed to span three key areas:

- ▶ There is a serious divide between certain European countries and industry on the topic of digital nexus, profit split and value attribution to markets and/or data.
- ▶ There is a strong opposition to levies and withholding taxes by nearly everyone, but for a few source country policy teams.
- ▶ The US and Asia are awaiting developments and not strongly pushing their opinions. The US is going through a complex and significantly broad tax reform process, only some of which is focused on these issues, and a lot of US attention will be on its own reform in the coming three to five months.

The OECD indicated that it would deliver a draft report in April 2018, and a final report before the end of April 2019 – a tough assignment, but the TFDE was very committed to hard work between now and then, and time will tell whether the OECD or the EU rise to the top of the policy discussion.

Concluding thoughts

The OECD, in its 2015 Action 1 report (which noted the possibility to use an equalization levy, as now being assessed in the EU, but which was ultimately not endorsed by the OECD), set out that the challenges of taxing digital activity would be most effectively addressed by work carried out under other BEPS Actions.

Those BEPS recommendations are approximately two years old, and implementation began in most countries only in 2016 or 2017; so at most we are only a year or so into assessing results.

Moreover, certain measures such as the OECD’s Multilateral Instrument (MLI) and the EU ATAD, both of which address the issues at hand, are only expected to broadly enter into force as of 2019 or later. Therefore, these measures are too new to objectively evaluate in terms of their effectiveness.

Additionally, there is no reason to believe that, following the introduction of the BEPS measures, the OECD’s Inclusive Framework members (which now totals 108 jurisdictions) will be lacking the means necessary to ensure that corporate profits are taxed in the appropriate source or residence jurisdiction. Arguably, any new activity fails to allow the efficacy of such measures to be accurately gauged.

13. “BEPS public consultation on the tax challenges of digitalisation” OECD website, <http://www.oecd.org/tax/beps/public-consultation-on-tax-challenges-of-digitalisation-1-november-2017.htm>, 1 November 2017.

The ECOFIN Council meeting on 5 December effectively cemented in place the European Commission's wishes (if not those of all Member States), well in advance of the scheduled release of the OECD report.

Any approach driven by the Commission that would effectively revise the PE concept in a way that is different from the current globally accepted norms under the work of the OECD, meanwhile, would have significant undesired consequences for the coherence of the global cross-border tax architecture. This is because, not least, there will be a need for the potential renegotiation of a host of bilateral tax treaties – right at the time that up to 100 treaty-amending choices are being made by more than 100 jurisdictions as a result of the existence of the OECD's MLI.

Saint-Amans concluded his keynote address to EY's International Tax Conference by saying, "You will have seen the Europeans say, 'We are impatient, and our people don't understand that some players don't pay any tax. The international principles have not kept pace with technological changes, and we must come to an agreement. We, at the OECD, strongly disapprove of unilateral measures. But it's going to be hard to tell countries not to move, if there is no prospect of any form of agreement.

"That's where we turn to the US, and hope that the US will send messages that there is the possibility of an agreement of new rules being developed in the next couple of years.

"I was in Japan ... to meet the finance minister and his G20 team. Japan is interested in making sure that in 2019 there will be a framework or some form of agreement. And [the OECD went] back to Washington to discuss that with the G20 finance ministers, and hope that we can have some prospects of political agreement, around which the technicians can deploy a technical solution."

So what's ahead? That, of course, is the million dollar question, as they say. The change in position that the above words would seem to indicate is certainly unexpected, given the vigor with which France drove the earlier debate. Again, the position of the US is underlined; as Saint-Amans also told the EY event, "maybe the highest source of uncertainty in today's environment – and this is what the Chinese delegate told the Forum on Tax Administration ... and in particular, told the US Tax administration – is US tax reform. Will or won't it take place? It will take place. The question is when. The system is broken. It needs fixing." [Editor's note: Saint-Amans words were spoken in advance of US tax reform passing]

There is much to be aware of in the coming months in relation to this reinvigorated discussion; as noted, the ECOFIN Council meeting on 5 December effectively cemented in place the European Commission's wishes (if not those of all Member States), well in advance of the scheduled OECD report. So we'll then see a response from the OECD in early 2018, where incidentally, Brian Jenn of the US Treasury is co-chair of the TFDE.

But one thing is for sure: for an issue that had largely floated into the background since 2015, the debate on digital taxation is moving at a disruptive pace. Let's hope this disruption does not result in an impediment to the amazing technological progress we have seen in recent years.



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EU blacklist, global ramifications

Why the EU's listing of non-cooperative jurisdictions for tax purposes may be a step too far



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“**N**aming and shaming” – and putting someone in isolation from their peers – are behaviour modification techniques that typically polarize any audience. Whether the topic at hand is effective parenting or global geo-political relationship management, there will be supporters and nay-sayers. Both sides will vehemently believe they are correct.

The European Commission no doubt considered this when preparing – and then announcing, on 5 December – a new listing of “non-cooperative jurisdictions for tax purposes.” Or, as it was instantly named by everyone outside that organization, the “tax blacklist.”

Tax blacklists are not new. Spain introduced one almost twenty years ago, while the OECD used a three-tiered “black” “gray” and “white” list approach in the wake of the global financial

The creation of a second listing of jurisdictions (who have all agreed to proactively make changes as a result of EU screening) represents a “grey list”, effectively tarring their reputation by association. That is unfortunate, and is seen by many as an over-bearing approach by the Commission.

crisis to try and drive increased transparency – but subsequently decommissioned it, due in part to widespread criticism. Brazil adopted one in 2010 and now uses it to target its anti-abuse measures at those it views as the worst offenders. And the OECD delivered a new blacklist to G20 leaders in 2017 – but couldn’t find anyone behaving badly enough to put on it.

High level impacts

The impacts of this latest European development – the delivery of a list of 17 jurisdictions¹ (reduced to 9 in late January 2018) with a further 8 escaping the list in order to give them time to recover from 2017’s Caribbean hurricanes – may be widespread and serious, and will be felt by countries and taxpayers alike.

Countries may find themselves the target of reduced inbound investment due to the sheer reputation risk (the “name and shame”) attached to being listed. They may also lose access to EU funding or guarantees, a matter of great importance to many jurisdictions, as well as finding that the listing finds its way into other relevant lists, both at EU level and elsewhere.

More broadly, some jurisdictions are livid at their inclusion, feeling that they tried to work collaboratively with the Commission, only to then find themselves present in the final listing.

A second set – some 47 jurisdictions, including Hong Kong, Switzerland, Turkey and Thailand, among others – feel that although the specific words were never used by the Commission, the creation of a second listing of jurisdictions (who have all agreed to proactively make changes as a result of EU screening) represents a “gray list”, effectively tarring their reputation by association. That is unfortunate, and is seen by many as an over-bearing approach by the Commission.

Taxpayers using the 17 listed jurisdictions are likely to find themselves sanctioned too, with either drastically enhanced reporting, scrutiny and tax audits or with new legislative measures that will increase their costs and reduce net income.

The background

Work on the listing began in July 2016. Requests for information were made of each jurisdiction and, in October 2017, letters were sent to all that were potentially affected, informing them of the outcome of the work. Where necessary, jurisdictions were requested to make a political commitment to address all deficiencies within a specified timeframe. Most jurisdictions engaged with the EU, taking steps towards resolving the issues identified; progress made on those commitments will be monitored. Some did not – or at least, not to the level desired by the EU.

Commitments made

Three key elements were used by the Commission in its screening process: tax transparency, fair taxation (i.e., the absence of what are described as “harmful” tax practices) and the jurisdictions’ implementation status in regard to the OECD’s BEPS recommendations.

Alongside the 17 – each of which has been given clear and unequivocal instructions on what must be changed in order to be de-listed – the 47 jurisdictions named as “committing to implement tax good governance principles” must also deliver on promises made in either 2018 or 2019. The commitments made by these countries effectively boil down to introducing the OECD norms on automatic exchange of information, transparency, and the minimum standards on BEPS, including on harmful tax practices. They have committed to do so before the end of 2018, or in case of developing countries, 2019. In fact, many jurisdictions had to make commitments in more than one of these areas.

Defensive measures

The European Commission say that in order to ensure coordinated action against those on the blacklist, EU Member States should apply at least one administrative measure in the area of tax, although the adoption of such defensive measures is not legally required. Defensive measures include reinforced monitoring of certain transactions, increased audit risks for taxpayers benefiting from the regimes at stake, and increased audit risks for taxpayers using structures or arrangements involving the relevant jurisdictions.

1. American Samoa, Bahrain, Barbados, Grenada, Guam, Korea (Republic of), Macao SAR, Marshall Islands, Mongolia, Namibia, Palau, Panama, Saint Lucia, Samoa, Trinidad and Tobago, Tunisia and United Arab Emirates

The notion of effectively being forced to implement the BEPS minimum standards or be blacklisted challenges the very notion of tax sovereignty. This is an area in which the Commission has received criticism in the past; now, it has effectively moved past prior bright lines, extending its reach into third countries all around the world. That is a dangerous notion.

Additionally, the Commission suggests that defensive measures of a legislative nature could be applied by Member States, including making certain costs non-deductible, applying enhanced Controlled Foreign Company rules, implementing new withholding tax measures, limiting any participation exemption use, putting in place switch-over rules, reversing the burden of proof, adopting special documentation requirements, and requiring the mandatory disclosure by tax intermediaries of specific tax schemes with respect to cross-border arrangements.

Member States, the Commission says, could also consider using the EU listing as a tool to facilitate the operation of relevant anti-abuse provisions, including as a basis for their own national blacklists. Many such “blacklists” are already in use in jurisdictions globally, including Belgium, Brazil, Italy, Mexico, and Spain, among others. Publication of the EU listing therefore raises the likelihood of non-EU countries also adopting the listing to supplement their own.

Other impacts

At a broad level, there may be reputation risks to companies using structures or transactions involving the 17 jurisdictions; indeed, analysis of large multinational businesses dealing with jurisdictions on the listing may occur from some quarters.

A further indirect impact is that the Commission has secured commitments from the 47 on the second listing that they will take significant action in order to be delisted. This includes implementing the spontaneous and automatic exchange of taxpayer information; securing membership of the Global Forum on Transparency and Exchange of Information for Tax Purposes (and securing a ‘satisfactory’ rating therein); amending or abolishing harmful tax regimes identified by the Commission; addressing EU concerns relating to the level of economic substance their tax benefits require in order to be secured and finally the taking up of membership of the Inclusive Framework on BEPS and, by consequence, implementing the BEPS minimum standards – though the Commission has also noted that this final commitment is not a specific requirement for delisting.

As a result of this last commitment, the Inclusive Framework on BEPS, for example, will grow by at least 12 members as a result, while at least six jurisdictions have agreed to implement the automatic exchange of information by 2018.

Looking forward

Time will tell whether any EU Member States adopt new counter-measure legislation; it should be expected that they will, although the listing is expected to further reduce in size as more jurisdictions make their best efforts to be delisted.

Furthermore, the Commission is also expected to drive additional work around the creation of a more binding, definitive approach to counter-measures in relation to the listing in 2018. This may also tie in to the European Parliament’s desire for Country-by-Country Reporting information to be made public in the future.

Moreover, it will be interesting to see what happens to the second listing of countries under close scrutiny; does that listing in fact become the new blacklist, in effect?

All things considered, the Commission may well believe that their intentions are good. But with one single document, they risk not only geo-political angst, but more tax uncertainty and higher likelihood of hastening the “global tax chaos” that we all fear looks set to occur.



Transparency

OECD issues Country-by-Country Reporting Handbook on Effective Tax Risk Assessment



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The first multilateral exchanges of Country-by-Country Reporting (CbCR) data in June 2018 will provide tax authorities with more detailed data about a company's global tax affairs than they have ever had.

The OECD recently published guidelines for tax risk assessment under CbCR, providing much-needed insight for tax authorities and taxpayers alike.

As tax administrations around the world prepare to start exchanging CbC reports next year, the OECD has released tax risk assessment recommendations it hopes will lead to greater transparency – not increased controversy.

The OECD publication released 29 September, "Country-by-Country Reporting: Handbook on Effective Tax Risk Assessment," sets out recommendations for national tax authorities to consider when introducing CbC reports into their existing tax risk assessment frameworks.

Businesses have expressed concerns in the lead-up to the CbCR introduction that the high-level data may be misinterpreted without the right context.

The first CbC data, which will start to be exchanged by 30 June, 2018, will provide tax authorities for the first time with a full breakdown of a multinational enterprise's (MNEs) revenue, profits, tax and other attributes by tax jurisdiction, significantly increasing the volume and scope of information available to them.

To date, more than 55 jurisdictions have introduced an obligation for MNEs to file CbC reports, according to the OECD, while over 1,000 exchange relationships between pairs of jurisdictions have been created.

Tax risks ahead

The responsibility now falls on tax authorities to ensure they make "effective and appropriate use" of the data contained in the CbC reports, according to the OECD. Used alongside other data collected by tax authorities and as a basis for additional inquiries, information gleaned from the CbC reports can play an important role in identifying transfer pricing and other risks.

Indeed, businesses have expressed concerns in the lead-up to the CbCR introduction that the high-level data may be misinterpreted without the right context.

But the OECD's handbook also "raises cautions about the risk that simplistic and misleading conclusions may be drawn if CbC reports are used in isolation."

The global tax picture

The detailed CbC information, the OECD says, will provide tax administrations with a better understanding of how local entities within their country fit within the structure of large and complex MNEs, the handbook. Moreover, tax officials will be able to carry out better risk assessments, identifying possible high-risk taxpayers and arrangements, and that tax administrations should also use the CbC data to identify those taxpayers that pose a lower tax risk – and change the types of compliance interventions made as a result.

Identifying patterns

Most of the time, tax authorities will need to compare the data contained in the CbC reports with two or more different sources of information, such as the transfer pricing master file, local file, and the authority's own knowledge and experience of the MNE's activities and risk behavior in order to find possible sources of tax risk. This also holds true for uncovering patterns that indicate high- and low-risk taxpayers.

Such patterns, according to the handbook, may be identified in a variety of ways, including:

- ▶ An MNE group's profile in a particular jurisdiction may be compared with that in other jurisdictions, with part of the group (e.g., a geographical region) or with the group as a whole.
- ▶ An MNE group's profile in a jurisdiction may be compared with that of a "typical" MNE group in the same sector (i.e., based on the profiles of all MNE groups operating in a particular sector).
- ▶ An MNE group's profile in a jurisdiction can be compared with CbCR information for the same jurisdiction in earlier periods, allowing a tax authority to identify changes in the nature or level of activity in a jurisdiction over time.

Risk profile

What is particularly interesting is that the handbook sets out a series of 19 specific risk indicators (i.e., analytics tests) that could be run across CbC data and used with other information to determine a MNE's overall level of tax risk.

For each risk indicator, a summary overview is also provided in the handbook, while an annex sets out what potential results could mean, as well as exploring other possible explanations.

The handbook's statement that the existence of CbC reports will "facilitate the development of multilateral components to the risk assessment of certain MNE groups, involving the tax authority from more than one jurisdiction" foreshadows the piloting of an International Compliance Assurance Program (ICAP) by a number of jurisdictions under the OECD's guidance (see page 28).

It should be expected that national tax administrations will, at a minimum, utilize the risk indicator tests as outlined in the report, while also supplementing them with their own.

As more and more tax administration processes become multilateral in nature, staying up to date with the risks and opportunities therein will be an important activity for MNE's.

The handbook represents the first publically-available information setting out exactly how tax authorities may use CbCR information to supplement their existing tax risk assessment protocols. It should be expected that national tax administrations will, at a minimum, utilize the risk indicator tests as outlined in the report, while also supplementing them with their own.

It's not often that taxpayers are granted any transparency into what tax authorities do with the tax and financial data submitted to them. So while it might not provide a complete picture, the handbook nonetheless provides useful guidance to those companies wishing to develop pre-submission tests to ensure their compliance risk assurance approaches are aligned with those likely to be adopted by the tax authorities – presumably exactly what the OECD is hoping.

19 risk factors identified in the CbCR handbook

1. The footprint of a group in a particular jurisdiction
2. A group's activities in a jurisdiction are limited to those that pose less risk
3. There is a high value or high proportion of related party revenues in a particular jurisdiction
4. The results in a jurisdiction deviate from potential comparables
5. The results in a jurisdiction do not reflect market trends
6. There are jurisdictions with significant profits but little substantial activity
7. There are jurisdictions with significant profits but low levels of tax accrued
8. There are jurisdictions with significant activities but low levels of profit (or losses)

9. A group has activities in jurisdictions which pose a BEPS risk
10. A group has mobile activities located in jurisdictions where the group pays a lower rate or level of tax
11. There have been changes in a group's structure, including the location of assets
12. Intellectual property (IP) is separated from related activities within a group
13. A group has marketing entities located in jurisdictions outside its key markets

14. A group has procurement entities located in jurisdictions outside its key manufacturing locations
15. Income tax paid is consistently lower than income tax accrued
16. A group includes dual resident entities
17. A group includes entities with no tax residence
18. A group discloses stateless revenues in Table 1
19. Information in a group's CbC Report does not correspond with information previously provided by a constituent entity

Source: OECD - <http://www.oecd.org/tax/beps/country-by-country-reporting-handbook-on-effective-tax-risk-assessment.htm>

2017 Tax risk and controversy survey series: Part III

2017 Tax risk and controversy survey series: Dimming the glare

For the EY 2017 Tax Risk and Controversy Survey Series, we surveyed 901 tax and finance executives representing more than 17 industries in 69 jurisdictions. In a series of reports, we analyze the survey's findings on what business taxpayers are seeing in practice in a variety of aspects across the tax lifecycle of planning, provision, compliance and reporting. In part 3 of the series, Dimming the glare, we explore emerging trends in tax controversy management.

In this new world order, it is critical that businesses have a cohesive approach to tax risk and controversy management. The BEPS initiative has given tax authorities new tools to combat perceived abusive tax structures and emboldened them to be more aggressive in challenging tax positions.

As governments continue to implement the BEPS Action items at varying speeds (and in sometimes inconsistent ways), and with tax authorities developing more sophisticated ways to obtain taxpayer data and enforce tax compliance, the international tax climate is likely to remain volatile for at least the next several years. This, in turn, means that businesses should expect to see more audits, more tax controversies and a higher possibility of double taxation.

Given this more-encompassing tax environment, it is evident that businesses are, in general, taking a more proactive approach to managing tax risk and controversy and are implementing more robust tax compliance processes, according to the 901 tax and finance executives in 69 jurisdictions who participated in the EY 2017 Tax Risk and Controversy Survey.



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Transparency

Global updates on tax transparency and disclosure since our last edition

Indian Tax Administration releases final rules on Country-by-Country reporting and Master File implementation

On 6 October 2017, the Indian Tax Administration issued draft rules for CbC reporting and the furnishing of the master file for public comments. Following the submission of public comments from various industry stakeholders, on 31 October 2017, the Indian Tax Administration issued the final rules for CbC reporting and the furnishing of the master file. The Final Rules contain a few administrative changes and clarifications.

<https://go.ey.com/2AhO3fH>

This article provides a non-exhaustive update on selected recent tax developments, set out in date order. The volume, speed and complexity of new developments continues to be high, and this article has been prepared for general informational purposes only. It is not intended to be relied upon as accounting, tax or other professional advice. Please refer to your advisors for specific advice.

Indonesia: Country-by-Country Reporting update

On 3 November 2017, EY published an update discussing various issues related to CbC Reporting in Indonesia.

<https://go.ey.com/2ych8sf>

United States announces withdrawal as an Extractives Industry Transparency Initiative (EITI) country

On 2 November 2017 the United States government announced that it was discontinuing implementation of the EITI standard, citing that US laws prevent it from meeting specific provisions of the EITI standard.

The Government of the United States is no longer an implementing country, but remains a supporter of the EITI internationally. Supporting governments are committed to promote good governance in the extractive industries across the world. A supporting country can support the EITI through financial, technical and political support at the international level and in implementing countries.

The United States' withdrawal letter is available on EITI website.

https://eiti.org/sites/default/files/documents/signed_eiti_withdraw_11-17.pdf

Cypriot Tax Authorities announce Country-by-Country Reporting Notification deadline extension

On 9 October 2017, the Cypriot Tax Authorities announced a one-month extension to the deadline for filing the Country-by-Country Reporting Notification for fiscal years starting on or after 1 January 2016. The new deadline is now 20 November 2017.

South African Revenue Service releases Public Notice concerning Country-by-Country reports, master file and local file

On 13 October 2017, the South African Revenue Service (SARS) released the final Public Notice concerning the filing of the Organisation for Economic Co-operation and Development Base Erosion and Profit Shifting Action 13-based Country-by-Country (CbC) report, master file and local file.

Following a round of public consultation, the timelines per the Public Notice are as follows:

- For years of assessment commencing on or after 1 January 2016 (filing is due within 12-months of the year-end):
 - A Reporting Entity (other than a Surrogate Parent Entity) that is a resident must submit a CbC report, master file and local file as discussed per SARS' Business Requirement Specification CbC and Financial Data Reporting. The aforementioned may affect South African headquartered multinationals that exceed the ZAR10b CbC reporting threshold.
 - The 1 January 2016 timeline may also apply to residents that are Constituent Entities.

- ▶ For years of assessment commencing on or after 1 October 2016 (filing is due within 12-months of the year-end):
 - ▶ A master file and local file are required where the aggregate of a person's potentially affected transactions for the year of assessment (without offsetting any potentially affected transactions against one another) exceeds or is reasonably expected to exceed ZAR100m, and that person is a resident.
 - ▶ The above may affect South African multinationals which do not qualify for the ZAR10b CbC reporting threshold, or South African subsidiaries of foreign multinationals.

Swiss Federal Council adopts ordinance on automatic exchange of Country-by-Country Reporting

In June 2017, the Swiss Parliament adopted a new federal law (the Law) regarding the automatic exchange of Country-by-Country (CbC) Reporting (CbCR) for multinational corporations. The deadline for a referendum regarding the Law expired on 5 October 2017.

On 29 September 2017, prior to the 5 October deadline, the Swiss Federal Council enacted an ordinance in relation to the Law, providing more clarity and detail regarding the implementation of CbCR in Switzerland. This ordinance will come into force on 1 December 2017.

Key elements of the Swiss CbCR regulations are:

- ▶ A consolidated revenue minimum threshold of CHF900 million before Swiss tax-resident entities are required to prepare and submit a CbC report.
- ▶ If this threshold is met or exceeded then Swiss tax-resident entities are required to submit a CbC report for fiscal years (FYs) starting on or after 1 January 2018.
- ▶ Voluntary filing is possible for Swiss Ultimate Parent Entities (UPEs) for FY16 and FY17.
- ▶ The content of Table 1 and Table 2 of the CbC report is consistent with the Organisation for Economic Co-operation and Development (OECD) guidance from Base Erosion and Profit Shifting (BEPS) Action 13.

- ▶ The FY18 CbC reports will be exchanged with partner countries beginning in 2020.
- ▶ Potential requests for a suspension of the automatic exchange of country-specific reports are to be addressed to the State Secretariat for International Financial Matters (SIF).

OECD publishes two handbooks on Country-by-Country reporting

The Country-by-Country Reporting: Handbook on Effective Implementation (the Handbook on implementation) is a practical guide to the key elements that countries need to keep in mind when introducing Country-by-Country (CbC) reporting in line with the Action 13 minimum standard. The report includes guidance on technical issues related to the filing, exchange and use of CbC reports, as well as on practical matters that tax authorities will need to address.

In the Country-by-Country Reporting: Handbook on Effective Tax Risk Assessment (the Handbook on tax risk assessment) the OECD sets out guidance on how each tax authority receiving CbC reports and transfer pricing master and local file documentation under Action 13 of the Base Erosion and Profit Shifting (BEPS) Action Plan may wish to consider using this information within their tax risk assessment programs, the types of risk assessment tests they may wish to consider utilizing, the challenges of effective use of CbC reports for tax risk management, and how to use CbC report alongside data from other sources.

<https://go.ey.com/2hNh52V>

Spain's new Form 232 updates existing reporting obligations for related party transactions, blacklisted jurisdictions and "patent box" regime

On 30 August 2017, Order HFP/816/2017 was published in the *Spanish Official Gazette* approving new Form 232, which updates certain existing reporting obligations in connection to: (i) related party transactions; (ii) transactions and shareholdings involving blacklisted jurisdictions; and/or (iii) related party transactions applying the Spanish "patent box" regime¹ for tax periods starting on or after 1 January 2016.

<https://go.ey.com/2wYPdP9>



Brazil

How will Brazil's application for OECD membership affect its tax policies?



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On 29 May 2017, the Brazilian Government formally applied to become a full member of the Organisation for Economic Co-operation and Development (OECD). The move is part of the Brazilian Government's wider plan to attract foreign investors as the country emerges from one of its worst recessions on record.

If the application is approved, Brazil would be the largest emerging economy in the OECD and the third Latin American country to join (after Mexico and Chile), as well as the first of the BRICS (Brazil, Russia, India, China and South Africa) to become an OECD member.

Brazil has had a working relationship with the OECD since the early 1990s, and this has intensified since 2009 as the agendas of the G20 (of which Brazil is a member) and the OECD have become more closely aligned.

The road to full membership could present some challenges, not least because Brazil's positions on certain tax policy issues diverge significantly from those of the OECD and its 35 member countries.

However, the road to full membership could present some challenges, not least because Brazil's positions on certain tax policy issues diverge significantly from those of the OECD and its 35 member countries.

Below is a high-level overview of Brazil's current relationship with the OECD, how its tax policies differ from OECD members, whether Brazil will need to revise those policies in order to accede to the OECD, and the next steps in its path to full membership.

Brazil's current relationship with the OECD

Brazil's collaboration with the OECD started in 1994, when it joined the OECD's Steel Committee, and gradually deepened. In 2007, Brazil and four other large emerging economies (China, India, Indonesia and South Africa) became "Key Partners" of the OECD, a status that enables those countries to participate in the work of the OECD's substantive bodies, with a view to possible full membership.

Today, Brazil participates in numerous OECD committees and working parties, including as an Associate of the Inclusive Framework on Base Erosion and Profit Shifting (BEPS) and as a member of the Global Forum on Exchange of Information and Transparency for Tax Purposes. In addition, Brazil has become an adherent to 31 OECD legal instruments, including the Convention on Mutual Administrative Assistance in Tax Matters.

Why has Brazil applied for full membership?

In the past, Brazil's decision-makers chose not to pursue full membership, as such a move would require the Government to make changes to domestic legislation in a number of areas, particularly in tax. However, with Brazil struggling to overcome a series of political crises and recover from a record-setting two-year recession, the centrist, pro-business government of President Michel Temer (who assumed office in August 2016 following the impeachment and removal from office of Dilma Rousseff on charges of manipulating the federal budget) is putting in place measures to attract foreign investment and boost growth. Applying for full membership to the OECD sends a strong signal that Brazil is seeking market-friendly policies.

What are the major differences between Brazil's tax policies and those of OECD member countries?

Brazil's transfer pricing policies are a key area of divergence. Brazil does not apply the arm's length standard for calculating transfer prices, as set out in the OECD's Transfer Pricing Guidelines.

Instead, it applies a formulary approach, with non-rebuttable fixed profit margins that are subtracted or added to the outcome of uncontrolled transactions (practiced price). The application of predetermined profit margins can, in some cases, lead to over- or undertaxation of transactions because the mark-up required by the Brazilian rules may be higher or lower than the profit actually derived by the taxpayer. The other country involved in the transaction may not make a corresponding adjustment when the profit allocated to the company located in Brazil does not reflect the arm's length standard (as prescribed by the OECD Transfer Pricing Guidelines).

Brazil's tax legislation, meanwhile, does not expressly provide for the elimination of double taxation arising from transfer pricing adjustments, and its double taxation treaties do not adopt the corresponding adjustment provisions under Article 9(2) of the OECD Model Tax Convention (OECD Model). Seeking double taxation relief through a treaty's mutual agreement procedure (MAP), if a treaty exists, generally has not been feasible, as Brazil to date has not resolved any treaty disputes via MAP (recent changes to Brazil's MAP practice are noted below). Multinational enterprises (MNEs) operating in Brazil have, to some extent, come to accept transfer pricing adjustments as a cost of doing business in Brazil – a solution that comes at the expense of reducing profit margins and reducing Brazil's competitiveness as a manufacturing location.

Brazil's treaty practice of applying withholding tax on payments remitted abroad for technical services – regardless of whether a permanent establishment (PE) exists – also departs from OECD norms. Taxpayers have long challenged Brazil's position, arguing that service payments should fall within the definition of business profits as established by Article 7 of the OECD Model, which limits source taxation to business profits made in direct connection with a PE.

For many years, the Brazilian tax authorities asserted that income related to technical services that did not involve a transfer of technology should be treated as "other income" under Article 21 of its tax treaties (which provides for withholding at source), rather than as "business profits" under Article 7, on the grounds that payments for technical services are classified under Brazil's domestic legislation as "revenue" and not as "profit" (it should be noted that Brazil's domestic legislation does not expressly define the term PE).

Brazil's position on MAP was, until recently, another area of divergence. Although its tax treaties contain MAP provisions, Brazil historically ignored requests to resolve treaty disputes via MAP

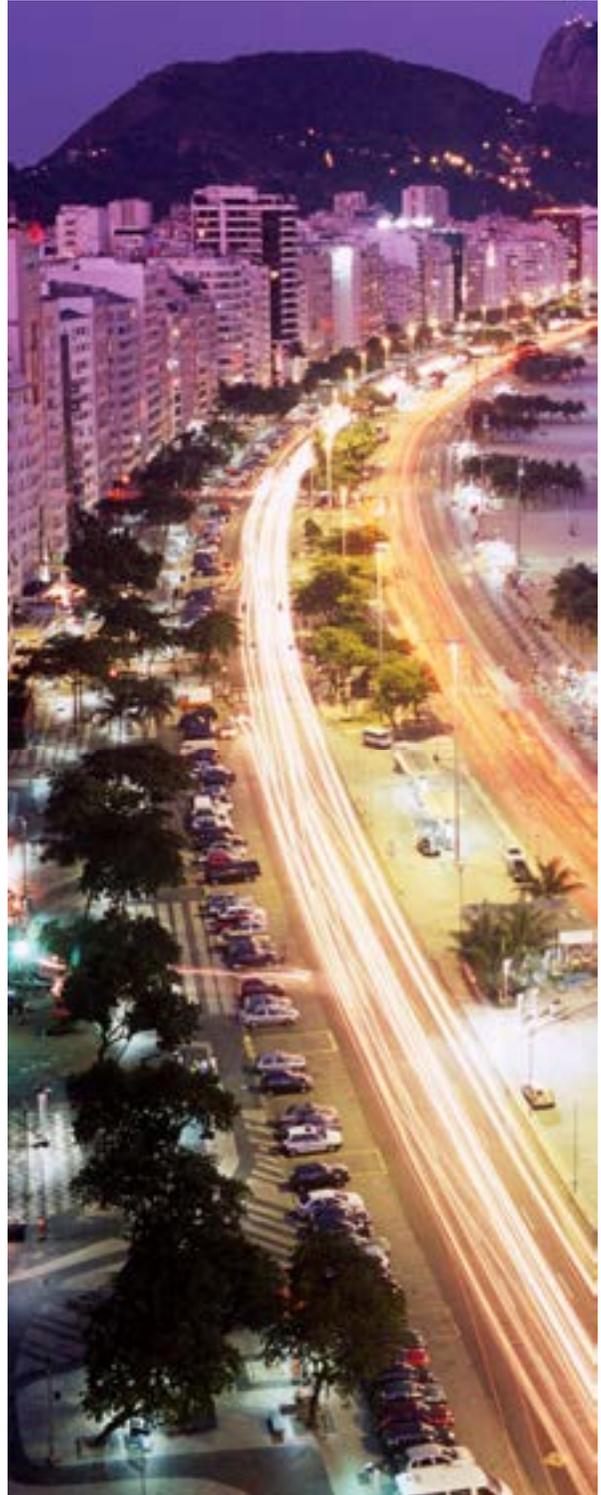
Brazil's Federal Supreme Court rejected the tax authorities' position in a 17 May 2012 decision (REsp 1161467/RS) involving an interpretation of the Brazil-Canada tax treaty. The court held that the treaty definition of business profits is broader than the domestic definition of taxable income and, therefore, Article 7 applied to payments remitted abroad for technical services performed without any transfer of technology.

Following that decision, the Brazilian tax authorities abandoned its "other income" position in an Interpretive Declaratory Act issued in June 2014. However, the government stated that, if technical services are included in the definition of "royalties" for treaty purposes (whether a transfer of technology is involved or not), then the royalty provisions of Article 12 (which permits withholding at source) are to apply, rather than Article 7. Moreover, the tax authorities adopted a very broad concept of "technical services," stating that such services cover any activity in which the service provider needs "skills, technique and training." In effect, Brazil preserved its right to tax fees for technical services (as well as administrative and similar services) at source. This unilateral approach to changing the application of tax treaties is not in line with the principles set forth in the Vienna Convention on the Law of Treaties (Vienna Convention), to which Brazil is a party.

Brazil's position on MAP was, until recently, another area of divergence. Although its tax treaties contain MAP provisions, Brazil historically ignored requests to resolve treaty disputes via MAP (as part of its BEPS commitments, Brazil last year published guidelines under which taxpayers can request that MAP be invoked; see below). Brazil's position was one of the reasons that Germany decided, in 2005, to terminate its tax treaty with Brazil.

Will Brazil need to change its tax regime if it joins the OECD?

In principle, the OECD would require Brazil to start accepting the arm's length standard, or, at least, accept the arm's length standard when compelled to do so under a treaty MAP provision. This would likely require Brazil to adopt the arm's length standard in its domestic legislation. However, this could be a difficult step for Brazil to take, as it would require the Brazilian tax authorities to deal with the subjectivity that the arm's length standard entails, rather than the formulary approach that Brazil currently uses. A potential alternative would be for Brazil to maintain its current transfer pricing legislation but use a different approach within the context of double tax treaty situations. One possibility would be to accept different profit margins (in effect, move to a rebuttable margin system), when doing so would result in a transfer price aligned with that under the arm's length standard.



The Brazilian tax authorities have said they have no current plans to sign the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS (MLI).

Regarding the taxation of technical services, Brazil would, in principle, need to start following the Vienna Convention and accept the proper use of Article 7, which would limit Brazil's ability to classify such services as royalties under Article 12. However, it is important to note that Brazil is currently renegotiating nearly 10 tax treaties. Brazil intends to include in those treaties the broader definition of royalties, which would cover fees from technical, administrative and similar services. Under this definition, such services are those whose execution depends on specialized technical knowledge, as well as administrative assistance or consultancy activities carried out by independent professionals, employees or automated structures with clear-cut technological content.

Accordingly, to the extent its tax treaties are amended as a result of bilateral negotiations to include the broader definition of royalties, Brazil would be permitted to levy tax at source on service fee remittances under those amended treaties. Nonetheless, with regard to its remaining tax treaties, Brazil would be required to change its position and follow the Vienna Convention by respecting the narrower definition of royalties (which would mean accepting the application of Article 7 and the limitation of a country's power to levy tax at source on the remittances of service fees).

What is Brazil's position on the OECD's BEPS recommendations? Would it need to change its position if it joins the OECD?

As a member of the G20, Brazil has committed to implementing the BEPS minimum standards, i.e., those pertaining to Actions 5 (Harmful Tax Practices), 6 (Treaty Shopping), 13 (Country-by-Country Reporting) and 14 (Dispute Resolution). Accordingly, Brazil would not need to change its approach if it becomes a full OECD member, as OECD and G20 members are legally required only to implement the four minimum standards and are not legally obligated to implement measures categorized as common approaches or best practices.

It should be noted that while Brazil is permitted to maintain its current practice against corresponding transfer pricing adjustments, as the provision of corresponding adjustments is only a best practice and not a requirement under Action 14, it will nevertheless be obligated to provide access to MAP in transfer pricing cases, as that is required by the minimum standard under Action 14. Indeed, Brazil has formally committed, as noted in the Final BEPS Report on Actions 8-10 (Transfer Pricing), to grant access to MAP to resolve cases of double taxation arising from the fact that Brazil does not adopt the arm's length standard.

As part of its commitment to implementing Action 14, Brazil's tax authorities in November 2016 published a Normative Instruction (NI 1,669/16), which provides guidance on the requirements and criteria for taxpayers to invoke MAP under a relevant tax treaty¹.

In this sense, and within the context of the BEPS peer review and monitoring process, Brazil's MAP practices will be subject to peer review in December 2018. It is therefore expected that Brazil will want to demonstrate a change in behavior – not only to demonstrate it is compliant with BEPS, but also that it is moving toward a more OECD-compliant approach to dispute resolution.

The Brazilian tax authorities have said they have no current plans to sign the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS (MLI). The MLI is a mechanism created under Action 15 to enable interested countries to swiftly amend their existing bilateral tax treaties in line with the treaty measures recommended under the BEPS project. For now, it appears that Brazil will continue amending its 32 tax treaties on a bilateral basis. In fact, on 21 July 2017, Argentina and Brazil signed a protocol amending their 1980 tax treaty, incorporating several BEPS recommended measures that would typically be covered by the MLI.

What are the next steps?

According to the OECD's Framework for the Consideration of Prospective Members (Framework), upon receiving a request for membership from a Key Partner, the OECD Secretary-General will prepare for the OECD Council's consideration a proposal inviting the Key Partner to enter into accession discussions and develop an accession roadmap. The Council (the OECD's decision-making body comprising one representative per member country, plus a representative from the European Commission) will determine whether to open membership discussions based on the Key Partner's willingness, preparedness and ability to adopt OECD practices, policies and standards.

Annex I of the Framework sets out the criteria on which the Council bases its decision whether to open accession discussions. That includes the prospective member's "state of readiness" in a number of areas, such as economic and public governance; how its policies, laws, regulations and practices are aligned with the measures and practices required by OECD legal instruments; the prospective member's position regarding the OECD's fundamental values as expressed in the OECD's vision statement; and its political commitment to the OECD's membership obligations.

¹See EY Global Tax Alert: <http://www.ey.com/gl/en/services/tax/international-tax/alert--brazil-publishes-normative-instruction-on-mutual-agreement-procedures-under-tax-treaties>

In light of the significant changes to Brazilian tax policy that could arise if Brazil becomes a member of the OECD, MNEs should closely monitor the accession process. It is expected that Brazil will have to change its positions on transfer pricing and the taxation of service fees as minimum conditions to joining the OECD.

If the Council agrees to open accession discussions, the Secretary-General will prepare an accession roadmap for adoption by the Council. The roadmap details the conditions, criteria and process for accession, including the in-depth reviews that must be carried out by various OECD technical committees. Once the technical reviews have been completed, the Secretary-General will present to the Council the technical committees' formal opinions, a final statement from the prospective member and a general report on the accession process with a recommendation. The Council's decision to extend membership must be unanimous.

Key takeaways

In light of the significant changes to Brazilian tax policy that could arise if Brazil becomes a member of the OECD, MNEs should closely monitor the accession process. It is expected that Brazil will have to change its positions on transfer pricing and the taxation of service fees as minimum conditions to joining the OECD.

It would be surprising if Brazil does not succeed in its application for OECD membership, given its status as a Key Partner and its active participation in joint G20/OECD initiatives, including the BEPS project. As a G20 member, there will likely be strong political pressure to approve Brazil for OECD membership. In tax matters, having Brazil join the OECD would be beneficial for all parties involved – OECD members could learn from Brazil's experiences in tax administration, particularly its technical prowess in advancing tax digitalization, while Brazil could draw on OECD standards and practices in building a path for sustainable and inclusive development.

Even if Brazil does not become an OECD member, taxpayers should expect to see changes to Brazil's MAP practices as a result of the BEPS initiative. Given Brazil's commitment under Action 14 to resolving treaty disputes by mutual agreement, an opportunity exists for MNEs to start applying for MAP prior to the peer review of Brazil that is scheduled to begin in December 2018.





The UK's new corporate criminal offense

Lessons learned so far



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The UK's new corporate criminal offense (CCO) of the failure to prevent the facilitation of tax evasion entered into force on 30 September 2017. The CCO, which was included in the Criminal Finances Act enacted on 27 April 2017, subjects business entities themselves to criminal liability if they fail to prevent those who act for them, or on their behalf, from criminally facilitating tax evasion. An offense by a corporate entity or partnership could result in its criminal prosecution, an unlimited financial penalty, a public record of conviction and potential implications on the ability to trade.

The CCO legislation is exceedingly broad and also has a wide-ranging extraterritorial effect. It applies not only to all entities in the world where the underlying tax is owed to HM Revenue & Customs (HMRC), but also to non-UK taxes where an entity is incorporated in the United Kingdom, has a place of business in the United Kingdom or has had any aspect of the offense(s) occur in the United Kingdom. Moreover, while the financial services sector is one of the industries at higher risk, the CCO legislation applies to all industries, and there are a number of risks that may permeate across many industries.

How does a CCO arise?

An offense occurs when an “associated person” – a person acting on behalf of a business (defined as a “relevant body”), such as an employee, agent or service provider – facilitates the evasion of tax of a third party while acting on behalf of the business. If the business cannot demonstrate that it had reasonable procedures in place to prevent its associated persons from facilitating tax evasion, then it could be subject to a corporate criminal conviction and an unlimited fine.

The “facilitation of tax evasion” concerns both UK tax evasion and foreign tax evasion offenses, again evidencing the global reach of the legislation. Businesses are now attempting to identify the potential ways in which their associated persons could potentially facilitate the tax evasion of third parties while acting on behalf of the business. Some hypothetical examples include:

- ▶ An employee of a UK-based multinational bank knowingly refers a corporate client to an offshore accounting firm with the express intention of assisting the corporate client to set up a tax-evading structure, enabling the client to
- ▶ evade either UK or foreign income tax.
- ▶ An agent acting for a business colludes with a customer to disguise the source country of origin of goods in order to reduce the level of duties paid when importing said goods.
- ▶ A salesperson agrees to mis-describe the nature of goods or services sold in order to enable the customer to obtain a more favorable tax treatment (for example, to claim a deduction as opposed to capital expenditure).
- ▶ A payroll administrator agrees to mask the true travel plans of a globally mobile executive to evade income tax due in another territory.
- ▶ A member of the accounts payable staff agrees to submit payment to a supplier’s bank account in a low- or no-tax territory in the knowledge that the income is not being declared.

What is a defense?

When there has been an instance of tax evasion, and it has been facilitated by an associated person acting on behalf of a business, the only defense against a prosecution is that the business had put in place reasonable procedures to prevent associated persons from facilitating tax evasion; or, that it was not reasonable to have expected the relevant body to have any prevention procedures in place.

“Reasonable” is, of course, a subjective term, and the level of effort required to meet this test will vary from business to business, subject to the level of the risk of facilitation by associated persons. HMRC has set out six “guiding principles” that businesses should consider when developing reasonable procedures to prevent associated persons from facilitating tax evasion.

Carrying out a risk assessment is a fundamental starting point for identifying the risks of facilitation in the business and evaluating how well existing controls may already address those risks. In essence, the risk assessment drives the response to the legislation: until a business identifies where its CCO risks may arise, it is impossible to know whether existing controls can sufficiently manage the risk.

Investing in a robust risk assessment can pay dividends in terms of building a proportionate response and demonstrating that any subsequent actions are grounded in the risks that the business faces. A robust risk assessment can also help minimize the unnecessary waste of resources.

When the CCO legislation was enacted in April 2017, many businesses at first did not appreciate the global reach of the legislation. However, as businesses have studied the CCO more closely, many have recognized that a risk assessment should be undertaken on a group-wide basis, given that trying to exempt parts of a global organization can quickly become impractical. Indeed, in a recent EY survey of more than 400 respondents, the highest proportion (38%) said their organization has approached their CCO risk assessment by reviewing their global operations; 24% of the respondents said they are reviewing their UK operations first and will move on to their global operations later. Our CCO readiness work with a number of companies to date provides several key insights.

Financial services

Given that HMRC has stated that the financial services sector is a sector it believes is at higher risk (and also given their prior experience in reacting to new multi-territorial requirements), in general, financial services businesses are, we believe, ahead of nonfinancial services businesses in terms of carrying out their risk assessments. And while businesses in the financial services sector carry out a diverse range of activities, some common risk factors have emerged. In particular, the wide range of bespoke financial products that financial services businesses may provide, and the close relationships that often develop between financial service providers and their clients, create a higher risk that an associated person will facilitate tax evasion, according to HMRC.

Based on our CCO readiness work with clients, businesses in the wealth and private banking sectors tend to have higher CCO risks. Small business banking can also present higher risks in some circumstances. Other higher-risk areas that have been identified include property and real estate investments and specific customer and investor types

Businesses in the financial services sector have a number of existing controls to leverage – the key question is how best to incorporate tax controls into their wider financial crime and compliance framework. The CCO risk assessments carried out by financial services businesses have tended to be very client focused; this makes sense, as this is where the higher risks lie in the banking area. However, it is equally important that financial services businesses include other business units – such as human resources, accounts payable, and supplier and vendor management – in their risk assessments.

Other sectors

For nonfinancial services businesses, a key question when identifying potential CCO risks is whether there are areas within the business that may increase the motive of associated persons to facilitate tax evasion. For example, could a desire to keep key customers happy create pressure to help a customer evade tax? Similarly, could a competitive “reward culture” lead individuals to help customers evade tax to secure their own bonus payments? On the supplier side, could the pressure to drive down costs in the supply chain lead to cost savings being delivered via the facilitation of tax evasion of a supplier?

Focusing on the motives of associated persons to potentially facilitate tax evasion has helped many of our clients to identify potential risk areas better. We are also seeing businesses assess whether there are robust controls regarding sales invoices. While many businesses have controls in place in respect of invoice values, existing controls often do not consider the risk of facilitating tax evasion through the mis-description of the goods and services provided, and those with responsibilities for processing payment and invoicing may not be aware of the red flags.

Activities with customers or suppliers in jurisdictions that have low tax transparency, low (or no) taxes, or higher risks of bribery or corruption naturally present additional risks that businesses must manage appropriately. A number of businesses have sought to build on their existing processes and controls to manage the risk of bribery and corruption, and address the identified risks for facilitating tax evasion.

Intermediaries and due diligence

The use of contractors and intermediaries may also create CCO risks, in our experience. Businesses should review their controls to manage any risk that a contractor should actually be treated as an employee (and thus pay higher tax) to ensure that nobody in the business has the opportunity (whether intentional or not) to facilitate a contractor’s tax evasion.

Furthermore, businesses should consider clarifying how an intermediary that is supplying contractors is managing the risk that it might be facilitating a contractor’s tax evasion, as an intermediary may possibly be classified as an associated person of the business, upon scrutiny.

Businesses are also assessing their due diligence procedures. Many already perform due diligence when considering with whom they want to do business and when carrying out merger and acquisition (M&A) activities; businesses should now include the facilitation of tax evasion risk in those due diligence procedures. Businesses might also find that other businesses they want to work with will want to know how they are managing their CCO risks.

Organizations should therefore be prepared to provide evidence on how those risks are being managed within their business. This is relevant to not only new and existing business relationships, but also in the context of due diligence related to potential M&A activity.

Beyond the risk assessment

Carrying out a CCO risk assessment can be a challenging exercise, and it may be tempting to think that the hard part is over once the risk assessment has been completed. It would be incorrect to do so, however. Businesses should instead sustain their commitment and momentum, which will enable them to implement necessary changes, maintain compliance in the long term and adapt to evolving requirements.

After completing their initial risk assessment, it is likely that many organizations may need to take follow-up actions, such as:

- ▶ Deep-dive risk assessment: where a lack of information or granularity has led an organization to conclude that a business unit should be treated as higher risk, performing a deep-dive assessment could aid the business in better identifying and quantifying risks (for example, in a global business unit, with varying processes around the world).
- ▶ Controls effectiveness testing: many organizations have not yet conducted controls effectiveness testing for CCO purposes, and are instead relying on existing testing and management information. Controls effectiveness should be considered as part of a longer-term implementation plan, either as part of the business’s existing processes or as a stand-alone process.

Businesses should now be looking to rapidly implement any changes needed to address risks identified across the business and put in place key controls identified by HMRC, including top-level commitment, training and due diligence on employees and third parties.

The ultimate goal should be to embed CCO reasonable prevention measures into an organization's business-as-usual model. If a business views this as purely a policy or training exercise, it is highly unlikely the business will be able to show it has reasonable procedures in place.

In the EY survey mentioned earlier, 50% of the respondents said they anticipate their implementation efforts will be "moderate" based on their organization's CCO risk assessment; 37% said their implementation efforts will be "minimal"; and 13% said theirs will be "significant" (see Figure 2). On the question of where they anticipate having to invest the most effort after performing a risk assessment, the top response was "updates to recurring business processes" at 37%, followed by "communication with key stakeholders and senior leadership" at 32%, and "training" at 24%.

The bigger picture

The CCO is a broad regime and affects many different business units, so it will be very important to involve all the different stakeholders across the business (including compliance, risk, legal and internal audit) when performing the risk assessment and when implementing any changes. Our experience from working with businesses across a range of sectors is that the risk assessment provides the platform to determine a reasonable and proportionate response.

For many businesses that have completed their risk assessment, they are confident that the existing control frameworks go a long way – but possibly not far enough – to address the risks identified.

The CCO does not discriminate between different tax types; in that regard, nor should a CCO risk assessment. Instead, the tax function should lead a process that addresses the CCO holistically and not in a piecemeal fashion.

Businesses operating outside the United Kingdom should also bear in mind that the CCO is a risk-based measure that necessitates a risk-based approach. Therefore, not all global companies will need a resource-intensive approach. Instead, they should adopt an approach that addresses the level of risk posed by their business with, and in, the United Kingdom and leverage the controls and procedures they may already have in place.

The United Kingdom is not the only country looking closely at tax evasion. The Organisation for Economic Co-operation and Development (OECD) held its Fifth Forum on Tax and Crime in London on 7-8 November 2017, publishing new recommendations on tackling tax and economic crime more effectively.

We are also seeing a range of other developments globally, including the wider introduction of tax evasion as an anti-money laundering offense and the use of data by regulators to identify tax evaders and other criminals. Ultimately, global organizations will need to consider all of these developments, and in our view, developing a robust approach to complying with the CCO can provide a solid platform for global compliance.

For some businesses, this may mean further developing their existing protocols. For other businesses, such protocols may need to be built from the ground up. But whatever the case, the clock is ticking, and all businesses must reach the point where they can confidently demonstrate that "reasonable procedures" are – and have been – in place.



Staying connected to US tax reform impacts

In today's environment, tax reform and other major policy proposals can develop (and change) quickly. Tax directors are under increased pressure to explain key tax reform and related policy developments to the C-suite and boards.

To help you navigate this rapidly evolving landscape, Ernst & Young LLP has launched Policy Perspectives: EY's rapid response series, addressing US tax reform and other major policy developments. When a major tax reform or other key policy development takes place, join our luminaries for a rapid response discussion of the development and what it means. With their experience as leaders in the US government and private sector, and on Capitol Hill, our team will give you the information you need to have informed discussions with key stakeholders – both inside and outside your organization.

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<https://go.ey.com/2k10AiB>

Jurisdiction	Corporate income tax (effective rate paid)					Personal income tax (highest marginal rate)				VAT/GST/sales tax			
	2017	2018	Notes	% of change in 2018	Indicator	2017	2018	% of change in 2018	Indicator	2017	2018	% of change in 2018	Indicator
Argentina	35%	30%	Corporate income tax rate decreases from 35% to 30% for fiscal years starting 1 January 2018 to 31 December 2019, and to 25% for fiscal years starting 1 January 2020 and onwards.	-14.3%	Decrease	35%	35%	0%	No change	21%	21%	0%	No change
Australia	30%	30%		0%	No change	47.0%	45%	-4.3%	Decrease	10%	10	0%	
Brazil	34%	34%		0%	No change	27.5%	27.5%	0%	No change	18.0%	18%	0%	No change
Canada	28.07%	37.87%	Simple average combined federal rate (15%) and provincial / territorial rate (varies) on general income. By province/ territory, combined rates range from 26.5% to 31%.	-0.71%	Decrease	54%	54%	0%	No change	5.0%	5%	0%	No change
China	25.0%	25%		0%	No change	45%	45%	0%	No change	17%	17%	0%	No change
France	33.3%	33.3%		0%	No change	45%	45%	0%		20%	20%	0%	No change
Germany	30%	30%		0%	No change	45%	45%	0%	No change	19%	19%	0%	No change
India	43.3%	43.3%	Domestic company income tax rate is 30% and will gradually be reduced to 25% over the next three years. Rate shown to left is for foreign companies, and is inclusive of surcharge and education cess. Watch for rate reduction in 2018 Union budget	0%	No change	30%	30%	0%	No change	12.5%	No change	0%	
Indonesia	25%	25%		0%	No change	30%	30%	0%	No change	10%	10%	0%	No change
Italy	24%	24%		0%	No change	43%	43%	0%	No change	22%	22%	0%	No change
Japan	29.97%	29.74%	29.74% is the effective tax rate when federal and local (Tokyo) taxes are taken into account.	0%	-0.77%	45%	45%	0%	No change	8%	8%	0%	No change
Mexico	30%	30%		0%	No change	35%	35%	0%	No change	16%	16%	0%	No change
Russia	20%	20%		0%	No change	35%	35%	0%	No change	18%	18%	0%	No change
Saudi Arabia	20%	20%		0%	No change	20%	20%	0%	No change	N/A	5%	N/A	Increase (new tax)
South Africa	28%	28%		0%	No change	41%	41%	0%	No change	14%	14%	0%	No change
South Korea	22%	25%	New tax bracket for income over KRW300 billion	0%	Increase	38%	38%	0%	No change	10%	10%	0%	No change
Turkey	20%	22%	22% for 2018, 2019 and 2020, effective 5 December 2017.	10%	Increase	35%	35%	0%	No change	18%	18%	0%	No change
United Kingdom	19%	19%		0%	No change	45%	45%	0%	No change	20%	20%	0%	No change
United States	39%	26%	Assumes average state taxes of 5%. Taxable years beginning after 2017 and before 2026	0.0%	No change	39.6%	37%	-6.6%	Decrease				

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