The G20 and the Organisation for Economic Co-operation and Development (OECD) are committed to finalizing work on the Base Erosion and Profit Shifting (BEPS) project in 2015.

Based on a 15-point action plan issued in July 2013, the project is already creating uncertainty in the global tax landscape for multinational corporations (MNCs) as many countries have begun to make BEPS-driven changes to their tax laws and administrative practices. Developments affecting MNCs are likely to intensify as the project nears completion and in the months that follow.

The BEPS project

The BEPS project, a G20-led initiative, is designed to address government concerns about the potential for MNCs to locate profits where they are subject to favorable tax treatment. The OECD is developing recommendations for changes in international tax laws and treaties that governments can implement to reduce the potential for base erosion and profit shifting activity.

Both OECD and non-OECD countries are participating in the BEPS project. Among the non-OECD countries that are involved in all aspects of the project are significant world economies such as Brazil, China and India. Participants from about a dozen developing countries, as well as groups representing countries in South America and Africa, are also providing input.

Project status

During the course of the BEPS project, the OECD has issued numerous documents and discussion drafts, held public consultations and webcasts and sought public input. The business community has submitted extensive comments on all the BEPS documents.

The OECD is planning to issue final reports in all 15 focus areas by October 2015. While there will be OECD follow-up work continuing into 2016 and beyond, attention will turn to countries as they decide whether and how to implement the OECD recommendations.
Why are the recommendations important?

The output from the BEPS project is largely in the form of recommendations for the design of countries’ domestic laws, as well as proposed changes to tax treaties. Broadly, the OECD’s recommendations include changes that would:

- Limit interest deductions
- Eliminate the benefits of hybrid financing arrangements
- Lower the permanent establishment standards for taxable presence in a country
- Place new restrictions on access to benefits of tax treaties
- Create new transfer pricing rules for intangible property
- Recharacterize taxpayers’ transactions through new approaches to transfer pricing
- Require more robust transfer pricing documentation
- Require new country-by-country reporting

Many countries are not waiting for the OECD to issue final recommendations and have already begun making changes to their tax laws and tax administration.

EY has catalogued BEPS-driven changes in laws and administrative practices in more than 50 countries since the beginning of 2014. For example, legislation in Mexico has included several BEPS-related changes. The United Kingdom has introduced a new Diverted Profits Tax aimed at addressing base erosion, and Australia recently announced proposals that would expand its general anti-avoidance rule to address avoidance of a taxable presence. The EU has amended a directive affecting the tax treatment of hybrid loans, which member states are already implementing by modifying domestic law. The EU also recently presented a package of tax transparency measures aimed at increasing information exchange between member states. China has issued transfer pricing rules on outbound related-party fee payments.

Long-term, as a result of the global focus on BEPS, MNCs can expect to face:

- Increased reporting obligations
- More scrutiny of intangible property ownership and financing structures
- A greater focus on the substance of a transaction and its alignment with the business
- Increased complexity in transfer pricing
- Further limitations on access to treaty benefits
- More (and more complex) controversy
- A need for more proactive engagement with tax authorities to gain certainty and avoid or resolve disputes

How should companies prepare?

Some specific steps companies can take to respond to BEPS-related developments include:

- Build consideration of potential BEPS impacts into current tax planning
- Re-examine supply chains
- Analyze current and future financing arrangements
- Consider APAs and other early engagement with tax authorities
- Share updates on the changing global tax environment frequently with management, the audit committee and other affected stakeholders

Conclusion

The international tax changes stemming from the OECD BEPS project will transform the global tax environment in which MNCs operate. Businesses that do not attempt to anticipate the impact of these changes may struggle to adapt to new approaches and comply with new rules. Now is the time to evaluate the potential BEPS pressure points for your business and develop plans for ensuring that your business models and structures are aligned with the new global tax mindset.

For more information on the BEPS project, see: http://www.ey.com/GL/en/Services/Tax/OECD-base-erosion-and-profit-shifting-project