

# MACFARLANES

## BEPS OVERVIEW

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The table below sets out a summary of the current status of the OECD G20 BEPS project as reflected in the final reports published in September 2015.

ACTION	KEY CONCLUSIONS	NOTES
1 – The digital economy	<ul style="list-style-type: none"><li>• The digital economy and its business models do not generate unique BEPS issues, but some of its key features exacerbate BEPS risks.</li><li>• No specific action points. Risks identified are to be taken into account in other actions.</li></ul>	<ul style="list-style-type: none"><li>• OECD to produce a report reflecting the outcome of the continued work by 2020.</li></ul>
2 – Hybrid mismatches	<ul style="list-style-type: none"><li>• Recommended change to domestic laws seek to eliminate the differences in the tax treatment of an entity or instrument under the laws of two or more tax jurisdictions that result in either a double deduction for the same expense or a deduction and no taxation.</li><li>• Primary rule denies deduction in paying country. If not applied in paying country, defensive rule will allow other country to include payment in taxable income or deny duplicate deduction.</li><li>• Proposals largely limited to intra group or connected party arrangements.</li><li>• Proposed treaty change to ensure that benefit of treaties granted to hybrid entities (which are not treated as taxpayers by either or both States that have entered into a tax treaty) are granted in appropriate cases but not granted where neither State treats under domestic law the income of such an entity as taxable income.</li><li>• Further treaty changes proposed to ensure that the changes to domestic legislation recommended do not conflict with the treaty position.</li></ul>	<ul style="list-style-type: none"><li>• UK legislation likely with effect from 1 January 2017.</li><li>• Treaty changes to be included in multi-lateral instrument.</li></ul>
3 – Controlled foreign companies	<ul style="list-style-type: none"><li>• Recommended six core principles for CFC legislation: defining CFCs, exemptions and thresholds, defining CFC income, computing CFC income, attributing CFC income and prevention and elimination of double taxation.</li><li>• No obligation to adopt new or revised CFC rules following BEPS.</li></ul>	<ul style="list-style-type: none"><li>• HMRC regards UK law as compliant with the six core principles.</li></ul>

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4 – Interest deductions	<ul style="list-style-type: none"> <li>• Proposed limit on net interest deductions to 10%-30% taxable EBITDA plus an optional group-wide third party net interest expense ratio.</li> <li>• Proposed some relaxations to the restrictions in low risk areas (such as a de minimis threshold).</li> </ul>	<ul style="list-style-type: none"> <li>• OECD to continue work on banking and insurance sectors which will need specific rules and a group wide ratio throughout 2016.</li> <li>• UK consultation paper published 22 October 2015. Legislation unlikely before 1 April 2017.</li> </ul>
5 – Harmful tax practices	<ul style="list-style-type: none"> <li>• Preferential tax rulings should only be available where a ‘substantial activity’ requirement is met (the ‘nexus approach’). This approach was developed in the context of patent box regimes and has been agreed by the Forum on Harmful Tax Practices.</li> <li>• Exchange of information in relation to tax rulings.</li> </ul>	<ul style="list-style-type: none"> <li>• On-going monitoring and review.</li> <li>• UK likely to amend patent box regime in 2016. Consultation published 22 October 2015.</li> <li>• Exchange of information to take place from 1 April 2016 for future rulings and exchange of certain past rulings to be completed by 31 December 2016.</li> </ul>
6 – Treaty abuse	<p>Proposed treaty changes:</p> <ul style="list-style-type: none"> <li>• Preamble to include statement regarding anti-abuse.</li> <li>• Treaty benefits to be subject to: <ul style="list-style-type: none"> <li>• US style limitation on benefits rule requiring a sufficient link between the entity and the state of residence; and/or</li> <li>• a general anti-abuse rule (a ‘principal purposes’ test).</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• To be included in the multi-lateral instrument, though countries may choose to amend their treaties bilaterally.</li> </ul>
7- Definition of permanent establishment	<p>Proposed treaty changes:</p> <ul style="list-style-type: none"> <li>• PE extended to include situations where intermediary activities are intended to result in the regular conclusion of contracts (designed to attack commissionaire-type structures).</li> <li>• Definitions of ‘preparatory’ and ‘auxiliary’ activities limited to exclude “core activities” (designed to address fragmentation of activities by MNEs).</li> </ul>	<ul style="list-style-type: none"> <li>• Additional work on attribution of profits to PEs to be carried out with guidance anticipated before the end of 2016.</li> <li>• New definitions to be included in the multilateral instrument.</li> <li>• May affect UK domestic law definition in non-treaty cases.</li> </ul>
8-10 – Transfer pricing	<ul style="list-style-type: none"> <li>• Aim is to align taxable with corresponding business, economic, value-creating activities.</li> </ul>	<ul style="list-style-type: none"> <li>• New consolidated guidelines to be published in 2017.</li> </ul>

ACTION	KEY CONCLUSIONS	NOTES
	<ul style="list-style-type: none"> <li>• Focus on identifying the entities that are assuming the full level of risk involved.</li> <li>• When considering intangibles, reduced emphasis on the legal ownership and focus on entities that perform the functions, control the economically significant risks and contribute assets to the creation of the intangible.</li> </ul>	
11 – Measuring and monitoring BEPS	<ul style="list-style-type: none"> <li>• Self-checking measure designed to ensure efficacy of the BEPS package.</li> <li>• Aim to improve and expand upon the available sources and the quality and quantity of data.</li> </ul>	<ul style="list-style-type: none"> <li>• On-going monitoring and review.</li> </ul>
12 – Mandatory disclosure	<ul style="list-style-type: none"> <li>• Recommended framework for the mandatory disclosure of aggressive or abusive transactions, arrangements or structures in order to increase information flow.</li> </ul>	<ul style="list-style-type: none"> <li>• UK already has DOTAS rules. Not clear whether further change will take place.</li> </ul>
13 – Transfer pricing documentation and country by country reporting	<p>Three-tier approach recommended:</p> <ul style="list-style-type: none"> <li>• MNEs to provide tax administrations with a master file containing high-level information regarding its global operations and TP policies;</li> <li>• MNEs to provide country-specific local files to relevant tax authorities containing detailed TP documentation specific to each country, identifying material related party transactions, amounts involved and the company's TP analysis; and</li> <li>• Large MNEs to file a country-by-country report, following a specified template, which sets out revenue, profits before income tax and income tax paid in each jurisdiction in which the MNE does business. Also includes details such as number of employees, retained earnings and tangible assets in each jurisdiction and identifies each entity within the group doing business in a particular jurisdiction.</li> </ul>	<ul style="list-style-type: none"> <li>• UK legislation in FA 2015. Draft regulations to take effect from 1 January 2016.</li> <li>• First data to be delivered to tax authorities by 31 December 2017.</li> <li>• First exchange of data by 30 June 2018.</li> </ul>
14 – Dispute resolution	<ul style="list-style-type: none"> <li>• Efforts to improve the Mutual Agreement Procedure (MAP) supported by a peer-based monitoring mechanism.</li> <li>• Encourage increased use of mandatory binding arbitration.</li> </ul>	<ul style="list-style-type: none"> <li>• A minimum standard for resolution of disputes under the MAP recommended, which includes that treaty obligations be implemented in good faith.</li> <li>• Some states, including UK, have committed to including binding arbitration in bilateral treaties.</li> </ul>
15 – Multi-lateral instrument	<ul style="list-style-type: none"> <li>• Treaty to make multiple changes to multiple bilateral treaties.</li> <li>• Intended to cover changes to hybrid mismatches, permanent establishments and treaty abuse.</li> </ul>	<ul style="list-style-type: none"> <li>• UK chairing the negotiations, which are to begin November 2015. Target for completion by end 2016.</li> </ul>