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Table of contents

| | |
|---|----|
| Acronyms and abbreviations | 5 |
| Chapter 1. Introduction | 7 |
| Chapter 2. Background | 9 |
| Chapter 3. Action Plan | 13 |
| A. Actions | 14 |
| (i) Establishing international coherence of corporate income taxation | 15 |
| (ii) Restoring the full effects and benefits of international standards | 18 |
| (iii) Ensuring transparency while promoting increased certainty and predictability | 21 |
| (iv) From agreed policies to tax rules: the need for a swift implementation of the measures | 23 |
| B. Timing | 24 |
| C. Methodology | 25 |
| (i) An inclusive and effective process: launching the OECD/G20 BEPS Project and involving developing countries | 25 |
| (ii) Efficient process | 26 |
| (iii) | |

Acronyms and abbreviations

| | |
|----------------|--|
| BEPS | Base erosion and profit shifting |
| BIAC | Business and Industry Advisory Committee to the OECD |
| CFA | Committee on Fiscal Affairs |
| CFC | Controlled foreign company |
| FDI | Foreign direct investment |
| FHTP | Forum on Harmful Tax Practices |
| GDP | Gross domestic product |
| MAP | Mutual agreement procedure |
| MNE | Multinational enterprise |
| OECD | Organisation for Economic Co-operation and Development |
| PE | Permanent establishment |
| TFTD | Task Force on Tax and Development |
| TUAC | Trade Union Advisory Committee to the OECD |
| UN | United Nations |
| VAT | Value added tax |
| VAT/GST | Value added tax/Goods and services tax |

Chapter 1

Introduction

Globalisation has benefited our domestic economies. Globalisation is not new, but the pace of integration of national economies and markets has increased substantially in recent years. The free movement of capital and labour, the shift of manufacturing bases from high-cost to low-cost locations, the gradual removal of trade barriers, technological and telecommunication developments, and the ever-increasing importance of managing risks and of developing, protecting and exploiting intellectual property, have had an important impact on the way cross-border activities take place. Globalisation has boosted trade and increased foreign direct investments in many countries. Hence it supports growth, creates jobs, fosters innovation, and has lifted millions out of poverty.

Globalisation impacts countries' corporate income tax regimes. As long ago as the 1920s, the League of Nations recognised that the interaction of domestic tax systems can lead to double taxation with adverse effects on growth and global prosperity. Countries around the world agree on the need to eliminate double taxation and the need to achieve this on the basis of agreed international rules that are clear and predictable, giving certainty to both governments and businesses. International tax law is therefore a key pillar in supporting the growth of the global economy.

As the economy became more globally integrated, so did corporations



shared principles and a network of thousands of bilateral tax treaties that are based on common standards and that therefore generally result in the prevention of double taxation on profits from cross-border activities. Clarity and predictability are fundamental building blocks of economic growth.

massive re-emergence of double taxation. In fact, if the Action Plan fails to develop effective solutions in a timely manner, some countries may be persuaded to take unilateral action for protecting their tax base, resulting in avoidable uncertainty and unrelieved double taxation. It is therefore critical that governments achieve consensus on actions that would deal with the above weaknesses

that is not includible in income by the recipient (and is not subject to taxation under controlled foreign company (CFC) or similar rules); (iv) domestic law provisions that deny a deduction for a payment that is also deductible in another jurisdiction; and (v)

of interest expense therefore should take into account that the related interest income may not be fully taxed or that the underlying debt may be used to inappropriately reduce the earnings base of the issuer or finance deferred or exempt income. Related concerns are raised by deductible payments for other financial transactions, such as financial and performance guarantees, derivatives, and captive and other insurance arrangements, particularly in the context of transfer pricing.

ACTION 4

Limit base erosion via interest deductions and other financial payments

Develop recommendations regarding best practices in the design of rules to prevent base erosion through the use of interest expense, for example through the use of related-party and third-party debt to achieve excessive interest deductions or to finance the production of exempt or deferred income, and other financial payments that are economically equivalent to interest payments. The work will evaluate the effectiveness of different types of limitations. In connection with and in support of the foregoing work, transfer pricing guidance will also be developed regarding the pricing of related party financial transactions, including financial and performance guarantees, derivatives (including internal derivatives used in intra-bank dealings), and captive and other insurance arrangements. The work will be co-ordinated with the work on hybrids and CFC rules.

Preferential regimes continue to be a key pressure area. In 1998, the OECD issued a report (OECD, 1998) on harmful tax practices in part based on the recognition that a “race to the bottom” would ultimately drive applicable tax rates on certain mobile sources of income to zero for all countries, whether or not this was the tax policy a country wished to pursue. Agreeing to a set of common rules may in fact help countries to make their sovereign tax policy choices. The underlying policy concerns expressed in the 1998 Report as regards the “race to the bottom” on the mobile income tax base are as relevant today as they were 15 years ago. However, the “race to the bottom” nowadays often takes less the form of traditional ring-fencing and more the form of across the board corporate tax rate reductions on particular types of income (such as income from financial activities or from the provision of intangibles). The BEPS report (OECD, 2013a) calls for proposals to develop “solutions to counter harmful regimes more effectively, taking into account factors such as transparency and substance.” In furtherance of this goal, the work of the Forum on Harmful Tax Practices (FHTP) will be refocused to develop more effective solutions.

over-capitalisation of lowly taxed group companies and from contractual allocations of risk to low-tax environments in transactions that would be unlikely to occur between unrelated parties.

Alternative income allocation systems, including formula based systems, are sometimes suggested. However, the importance of concerted action and the practical difficulties associated with agreeing to and implementing the details of a new system consistently across all countries mean that, rather than seeking to

to address it. The work will also involve assessing a range of existing data sources, identifying new types of data that should be collected, and developing methodologies based on both aggregate (e.g. FDI and balance of payments data) and micro-level data (e.g. from financial statements and tax returns), taking into consideration the need to respect taxpayer confidentiality and the administrative costs for tax administrations and businesses.

Transparency on certain tax planning/transactions is also needed.

- Actions to be delivered *in two years* relate to CFC rules, interest deductibility, preventing the artificial avoidance of PE status, the transfer pricing aspects of intangibles, risks, capital and high-risk transactions, part of the work on harmful tax practices, data collection, mandatory disclosure rules, and dispute resolution.
- Actions that may require *more than two years* include the transfer pricing aspects of financial transactions, part of the work on harmful tax practices and the development of a multilateral instrument to swiftly implement changes to bilateral treaties. Although these actions are considered as key items of the Action Plan, it is recognised that this work will have to be developed in different stages, starting with a thorough analysis of the issues.

Annex A contains tables summarising the different actions and indicating the expected timeline for completing them.

C. Methodology

The BEPS project marks a turning point in the history of international co-operation on taxation. As the current consensus-based framework is at risk, it is critical that a proper methodology be adopted to make sure that the work is inclusive and effective, takes into account the perspective of developing countries and benefits from the input of business and the civil society at large.

(i) An inclusive and effective process: launching the OECD/G20 BEPS Project and involving developing countries

Accomplishing the actions set forth in this Action Plan requires an effective and comprehensive process that involves all relevant stakeholders. To this end, and in order to facilitate greater involvement of major non-OECD economies, the “BEPS Project” will be launched. In light of the strong interest and support expressed on several occasions by the G20, it is proposed that interested G20 countries that are not members of the OECD will be invited to be part of the project as Associates, i.e. on an equal footing with OECD members (including at the level of the subsidiary bodies involved in the work on BEPS), and will be expected to associate themselves with the outcome of the BEPS Project. Other non-members could be invited to participate as Invitees on an ad hoc basis.

Developing countries also face issues related to BEPS, though the issues may manifest differently given the specificities of their legal and administrative frameworks. The UN participates in the tax work of the OECD and will certainly provide useful insights regarding the particular

concerns of developing countries. The Task Force on Tax and Development (TFTD) and the OECD Global Relations Programme will provide a useful platform to discuss the specific BEPS concerns in the case of developing countries and explore possible solutions with all stakeholders. Finally, existing mechanisms such as the Global Fora on Tax Treaties, on Transfer Pricing, on VAT and on Transparency and Exchange of Information for Tax

Overview of the actions and timelines

This annex contains summary tables indicating the timeline for the actions included in the Action Plan.

Table A.1. Summary of the BEPS Action Plan by action

| Action | Description | Expected output | Deadline |
|--|---|-----------------|----------|
| 1 – Address the tax challenges of the digital economy | <i>Identify the main difficulties that the digital economy poses for the application of existing international tax rules and develop detailed options to address these difficulties, taking a holistic approach and considering both direct and indirect taxation. Issues to be examined include, but are not limited to, the ability to tax digital products and services.</i> | | |

| Action | Description | Expected output | Deadline |
|--|--|-----------------|----------|
| <p>2 – Neutralise the effects of hybrid mismatch arrangements</p> | <p><i>Develop model treaty provisions and recommendations regarding the design of domestic rules to neutralise the effect (e.g. double non-taxation, double deduction, long-term deferral) of hybrid instruments and entities. This may include: (i)</i></p> | | |
| | | | |

| Action | Description | Expected output | Deadline |
|--|--|--|-----------------------|
| <p>7 – Prevent the artificial avoidance of PE status</p> | <p><i>Develop changes to the definition of PE to prevent the artificial avoidance of PE status in relation to BEPS, including through the use of commissioner arrangements and the specific activity exemptions. Work on these issues will also address related profit attribution issues.</i></p> | <p>Changes to the Model Tax Convention</p> | <p>September 2015</p> |
| <p>8 – Assure that transfer pricing outcomes are in line with value creation: intangibles</p> | <p><i>Develop rules to prevent BEPS by moving intangibles among group members.</i></p> | | |
| | | | |
| | | | |

| Action | Description | Expected output | Deadline |
|---|---|-----------------|----------|
| 11 – Establish methodologies to collect and analyse data on BEPS and the actions to address it | <i>Develop recommendations regarding indicators of the scale and economic impact of BEPS and ensure that tools are available to monitor and evaluate the effectiveness and economic impact of the actions taken to address BEPS on an ongoing basis. This will involve developing an economic analysis of the scale and</i> | | |
| | | | |

| Action | Description | Expected output | Deadline |
|---|--|-----------------------------|----------|
| 13 – Re-examine transfer pricing documentation | <i>Develop rules regarding transfer pricing documentation to enhance transparency for tax administration, taking into consideration the compliance costs for business. The rules to be developed will include a requirement that MNE's provide all relevant governments with needed information on their global allocation of the income, economic activity and taxes paid among countries according to a common template.</i> | Changes to Transfer Pricing | 12/4/14 |
| | | | |
| | | | |

Table A.2. Summary of the BEPS Action Plan by timeline

| BY SEPTEMBER 2014 | | Expected Output |
|---|---|--|
| Action | Description | |
| Address the tax challenges of the digital economy | <p>Identify the main difficulties that the digital economy poses for the application of existing international tax rules and develop detailed options to address these difficulties, taking a holistic approach and considering both direct and indirect taxation. Issues to be examined include, but are not limited to, the ability of a company to have a significant digital presence in the economy of another country without being liable to taxation due to the lack of nexus under current international rules, the attribution of value created from the generation of marketable location-relevant data through the use of digital products and services, the characterisation of income derived from new business models, the application of related source rules, and how to ensure the effective collection of VAT/GST with respect to the cross-border supply of digital goods and services. Such work will require a thorough analysis of the various business models in this sector.</p> | Report identifying issues raised by the digital economy and possible actions to address them |
| Neutralise the effects of hybrid mismatch arrangements | <p>Develop model treaty provisions and recommendations regarding the design of domestic rules to neutralise the effect (e.g. double non-taxation, double deduction, long-term deferral) of hybrid instruments and entities. This may include: (i) changes to the OECD Model Tax Convention to ensure that hybrid instruments and entities (as well as dual resident entities) are not used to obtain the benefits of treaties unduly; (ii) domestic law provisions that prevent exemption or non-recognition for payments that are deductible by the payor; (iii) domestic law provisions that deny a deduction for a payment that is not includible in income by the recipient (and is not subject to taxation under controlled foreign company (CFC) or similar rules); (iv) domestic law provisions that deny a deduction for a payment that is also deductible in another jurisdiction; and (v) where necessary, guidance on co-ordination or tie-breaker rules if more than one country seeks</p> | |

| BY SEPTEMBER 2014 | | Expected Output |
|--|--|-----------------|
| Action | Description | |
| Develop a multilateral instrument – phase 1 | <i>Analyse the tax and public international law issues related to the development of a multilateral instrument to enable jurisdictions that wish to do so to implement measures developed in the course of the work on BEPS and amend bilateral tax treaties. On the basis of this analysis, interested Parties will develop a multilateral instrument designed to</i> | |

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