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Fight against tax loopholes – the BEPS action plan of the OECD

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Base erosion and profit shifting - or BEPS for short – refers to the legal practice of global companies moving sales and profit, for example by smartly setting internal transfer prices between permanent establishments in different countries, in such a way that their tax burden is minimised on the whole. This is enabled by tax regulations (tax rates and taxable events) and their actual implementation differing, sometimes significantly, between countries.

Such practice can lead to the following distortions of competition:

- Local small and medium-sized businesses do not have this opportunity to "reduce their tax burden", and suffer a competitive disadvantage as a result.
- Private companies utilise the social and economic infrastructure provided by the state at certain production locations without making appropriate contributions towards their improvement and maintenance through taxes. In other countries ("tax havens"), tax revenues accrue without being offset by corresponding services from the state ("windfall profits").

BEPS initiative of the OECD

To take action here against distortions of competition that cause macroeconomic damage, the OECD and G20 countries as well as emerging and developing countries grouped together in the BEPS project three years ago. Germany has been one of the most significant supporters of this project from the start. The primary objective was for taxation to take place at the location of the business activity and the economic value added.

In early October 2015, the OECD published a 15-point action plan with recommendations for the organisation of tax systems in the countries as a result of this initiative. The key elements of the action plan are as follows:

- Governments should inform each other promptly about individual tax arrangements with companies (tax rulings) as a matter of obligation in the future.
- With country-by-country reporting on certain corporate performance figures (profit, taxes, business activities), companies will be obliged to create more transparency to make it easier to identify transfer prices that do not correspond to market standards.
- Redesigning deduction restrictions can prevent companies knowingly financing themselves excessively through external financing in order to deduct high interest payments from the profit. The principle of an interest barrier should be implemented worldwide.
- Undesired leeway in international tax law will be removed and agreements – originally to avoid double taxation –will be revised in particular to curb double non-taxation.

Developing countries and BEPS

Developing countries suffer particularly from base erosion and profit shifting because they are often especially dependent on corporate taxes to generate their own income.

More than 80 developing countries and other non-OECD countries, as well as two regional tax organisations, the African Tax Administration Forum (ATAF) and the Inter American Center of Tax Administrations (CIAT) have got involved in the OECD initiative.

Together with other international organisations and regional tax organisations, the OECD Secretariat has developed toolkits to support developing countries in implementing the measures.

What are the next steps?

The implementation of the new regulations in the countries as well as their effectiveness in practice will continue to be closely observed by the OECD. The international community has also agreed to continue the work. Germany will ensure that the international collaboration in tax matters is further expanded. To this end, double taxation agreements, of which there are 3,500, must be changed, amongst other things. A multilateral agreement is to be drafted which "overwrites" or supplements existing double taxation agreements and implements the BEPS recommendations across the board so that not every contract has to be renegotiated. A corresponding draft will be prepared by the end of 2016.

Conclusion

The Heads of State and Government of the twenty most important economies in the world (G20) reached an agreement on the set of measures in Antalya. It remains to be seen whether the countries implement the regulations and whether the coordination between the tax authorities will actually improve in the future. Nevertheless, the close and public monitoring by the OECD will contribute towards harmonising tax regulations and closing tax loopholes on a step-by-step basis. Looking back at the last three years of the project, it is evident that the countries are ready to intensify their cooperation. In any case, the BEPS project represents a starting point for international tax policy. ■