



# 2016 LOOK-AHEAD

## BEPS implementation to dominate international tax landscape in 2016

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With the final deadlines for the OECD's BEPS Project falling at the end of this year, 2016 was always going to be a year dominated by questions about implementation. While BEPS-related activity is not the only issue on the horizon, that alone will ensure multinationals are kept busy over the next 12 months. Joe Stanley-Smith and Matthew Gilleard look through the peephole to analyse taxpayer hopes, fears and expectations for the year ahead.

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### US

From the outset of the BEPS Project in 2012, stakeholders realised that – as with any global initiative – the role of superpowers like China and the US would be critical to the success of the project as a whole.

Should the US fail to commit to the core principles of BEPS, many feel that the effectiveness of the whole project could be at risk. Nobody disputes that the US is in need of comprehensive tax reform – particularly in the field of international tax – but whether multilateral work on BEPS will be *a* trigger or *the* trigger for this is difficult to predict, particularly with a capricious election due in November.

Under the Obama administration, any progress is likely to be slow, particularly given the fractious legislative environment on Capitol Hill and the possibility of a government shutdown. However, the inevitability that anti-BEPS legislation will radically alter the international tax landscape undoubtedly provides a greater impetus for cross-party cooperation towards tax reform.

“The prospects for BEPS implementation are still unclear,” says Jeffrey Tolin, partner at Hogan Lovells in the US. “Legislation will

be required to adopt many of the changes. Both the House and the Senate held hearings on BEPS [on December 1] and initial reactions in Congress are best described as mixed. I am not sure whether there will be any momentum for change.”

This is not simply a matter of American obstinance. The US corporate tax system “is dramatically different from the systems in place in countries in Europe and elsewhere, both in terms of the corporate tax rate and in terms of the approach for taxing global income”, says Barbara Angus, US international tax policy leader for EY.

With a corporate tax rate of up to 39.5% that is far higher than the OECD average, and an outlying system which taxes resident companies on worldwide earnings, the US tax environment would be affected more than most by many of the BEPS measures. Indeed, some stakeholders are viewing the entire BEPS project as an ‘anti-US’ initiative.

“The BEPS Project final recommendations issued this year, coupled with the present European Commission investigation into the alleged receipt of illegal state aid by mostly American companies, expose what appears to be an extremely disturbing and multi-

faceted attack, targeted specifically at American companies,” said Congressman Charles Boustany, who sits on the tax-writing House Ways and Means Committee.

Tax justice campaigners, however, respond by levying the accusation that this can only be true to the extent that US companies are the ‘worst’ perpetrators of BEPS-related activities.

Boustany acknowledged that congressional inaction on reforming US tax legislation – the tax code was last overhauled in 1986, and the distance travelled since then from a digitalisation perspective, starting with the work of Sir Tim Berners-Lee, can only be described as ‘considerable’ – is a major reason for anti-BEPS actions having arguably the biggest impact in the US.

“Ladies and gentlemen, we are out of time,” he admits. “We have had nearly three decades of procrastinating on tax reform.”

With this in mind, any disproportionate impact of BEPS deliverables on US multinationals will largely be down to US legislative inaction since 1986. In short: blame Washington.

Angus says the aspects of the US corporate tax system that are different from those of major trading partners will become more acute in the post-BEPS environment.

“Many of the objectives and principles with respect to tax reform are points of common ground. If lawmakers can build on this foundation in 2016 to expand the areas of agreement, there is real hope for tax reform in 2017,” she says.

Whatever the progress towards domestic tax reform, BEPS brings the same concerns for US taxpayers as it does around the world: uncertainty, and an almost inevitable increase in tax disputes, both domestically and for US companies doing business overseas.

“Companies will need to stay informed about developments in all the countries where they operate or invest – they will need to anticipate both legislative and administrative changes,” says Angus. “Due consideration should be given to increasing proactive engagement with tax authorities in order to gain some certainty through upfront agreements such as APAs. Companies also will need to be communicating with internal stakeholders regarding the shifting environment.”

Independently of BEPS (though possibly aided by multilateral instrument discussions: see Action 15, page 46), the US will also see a greater focus on inversions, particularly in the wake of Pfizer’s \$160 billion acquisition of Allergan (see Deals, page 8).

“The Obama administration continues to chip away at these transactions with both definitional and operative rules, but it has made clear that it believes more needs to be done by legislation,” says Angus. “Some of this might also be done through the treaty process, as the US has revised its model treaty to provide for, among other things, special rules to deny benefits to inverted groups.”

### Latin America

“The most significant international taxation issue in the region during next year will be the domestication process of OECD-G20 BEPS recommendations, including the adoption of the not-yet-finalised multilateral agreement,” says Guillermo Teijeiro, partner at Teijeiro & Ballone, who fears that BEPS implementation – and the associated political challenges – will prove to be a “complex process” and one that could be “beyond the reach and technical capabilities of less developed economies in the region”.

In Latin America, as in other jurisdictions around the world, the complexities of implementing standardised measures to combat

BEPS are compounded by the fact that national governments have chosen to act unilaterally in recent years.

“Significant BEPS-flavoured legislative changes have occurred in LatAm in recent years, including OECD (Chile, Mexico) and non-OECD countries (for example, Brazil, Colombia and Peru), comprising tax measures even beyond the content of the 15 OECD actions, and basically aimed at improving transparency through exchange of information,” says Teijeiro.

In line with such aims, countries in the region have also been working to prepare for effective implementation of automatic exchange of information either under the new OECD Standard on Transparency and Automatic Exchange of Information, or FATCA, under IGA 1 or 2 models.

“The Chilean 2014 corporate amendment included the introduction of GAARs and CFC rules, as well as newly-enacted thin cap rules and indirect capital gains taxation. The Mexican 2014

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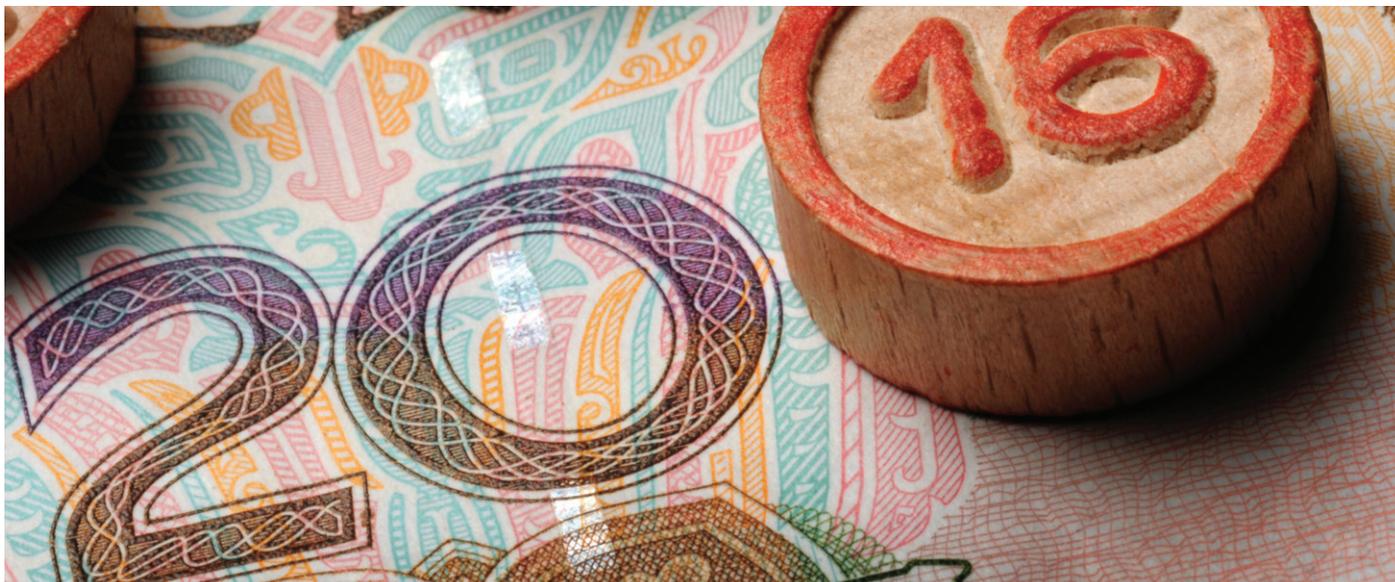
tax reform included, *inter alia*, a defensive rule against double deduction of outbound payments from Mexican corporations to their foreign controlling partners; the disallowance of interest, royalties and technical assistance fees paid to foreign beneficiaries which are non-taxable on these items of income in their home countries; and a subject-to-tax rule that conditions the granting of benefits to treaty-partner residents.”

“In a surprising move aligned with Action 12 of the OECD-G20 Plan, in recent months the Brazilian government proposed rules for the disclosure of aggressive tax planning schemes which are still struggling at the Congressional level through heavy criticism of a constitutional nature,” says Teijeiro.

In a similar vein, Argentina has intensified the application of its longstanding GAAR to cross-border deals (particularly to intra-group deals), as well as scrutiny of business deals in a treaty context. Application of domestic GAARs in a treaty setting is expressly contemplated in recent tax conventions, such as in the memorandum of understanding that has been annexed to treaties with Spain and Chile – though the treaty with Chile is not yet in force.

But national action in Latin America has not stopped there.

“The Colombian SAAR – an overreaching thin-cap rule – introduced in 2013, as well as the Peruvian 2012 reform which included, *inter alia*, a deemed or constructive dividend distribution upon the reduction of capital, new GAARs not yet fully implemented, and indirect capital gains taxation, completed the picture of anti-base eroding LatAm recent measures with which BEPS final



China will be a key player in BEPS implementation in 2016

reports should be reconciled while domesticated in a process which will start in 2016 but will surely take longer,” says Teijeiro.

Indeed, any reforms enacted in the area of anti-base erosion now need to be reconciled with the final OECD deliverables through 2016 and beyond.

The G20 Antalya Summit communique calls for a “widespread and consistent implementation” of BEPS final outcomes, but national legislators are not starting with a blank canvas. The situation pre-implementation is more akin to a group of painters being given the same set of brushes and paint-by-numbers manual, despite coming from different artistic backgrounds and standing in front of easels holding non-uniform base layers.

“Legislators will be faced with the policy decision of maintaining the existing vernacular approaches – perhaps consisting in measures that have proved to be effective in the past – or replacing them altogether with OECD-G20 newly-issued recommendations,” says Teijeiro.

The OECD would have preferred no unilateral action, but some countries could not wait for the final BEPS outcomes, instead choosing to act to protect their tax base unilaterally in advance of that.

Another implementation hurdle could come in the form of countries cherry-picking those parts of the final recommendations that are beneficial from a national revenue perspective, leading to inconsistencies and further mismatches.

A particular challenge for Latin American countries could come in the form of the Action 1 deliverables in relation to the digital economy, which Teijeiro says deserves special attention because “it is not difficult to imagine that LatAm countries will soon start applying indirect taxes on, and grasping income from, digital economy manifestations”.

“The door appears to be open for LatAm economies to grasp income from digital economy activities, but different responses in terms of available tools might stretch jurisdictional principles beyond an acceptable reach, as well as catastrophically affecting cross-border remote trades.”

Aside from adapting to developments in the digital economy by broadening the scope of indirect taxation, the worldwide trend towards passing voluntary disclosure schemes has reached Latin America and will provide taxpayers with opportunities for regularising their affairs throughout 2016.

Teijeiro expects to see a number of tax amnesties during 2016 as the transition to full transparency under automatic exchange of information continues.

“There are currently regimes in force in Chile and Colombia, and proposed legislation being considered in Argentina, Brazil and Mexico as a one-time opportunity for taxpayers to come forward before entering full transparency through automatic exchange of information, will probably be passed in 2016,” says Teijeiro.

## China

As alluded to, another key player in the BEPS process is China. While there may be fewer legislative obstacles to BEPS implementation than in the US, the country is also going through several other gargantuan tax reforms, with new provisions such as Bulletin 7 governing the calculation of capital gains, and the implementation of FATCA. The country’s indirect tax system is expected to be fully up-and-running in 2016 as well, with the VAT roll-out to the remaining sectors expected to be completed next year.

“We’re pretty much at the last phase of the VAT programme,” says Roberta An Chang of Hogan Lovells. “Telecommunications joined the VAT a while ago, so now you have, I think, only two or three big categories, including real estate and consumer services, that haven’t joined.”

Both taxpayers and the tax authorities are still struggling with VAT due to a dearth of experience dealing with the tax in China. It is therefore important that both sides, when considering industries which are yet to make the transition to VAT, learn from other sectors and regions which have already crossed over.

A key sector which is yet to become fully VAT-able is real estate, where VAT rules are generally more complex. The authorities have wisely left this until the end of VAT implementation to

allow companies to get up to speed – but taxpayers still have a lot of catching up to do.

Changes on this scale bring challenges for companies beyond just the tax department. Preparing other parts of the business to ensure 2016 changes are well-flagged is something that tax directors and CFOs should be working on now.

“What I see with a lot of clients is their finance people don’t know anything about VAT, that’s why when the notice comes out and says ‘effective immediately’, they don’t know what to do,” says An Chang.

Adding BEPS into the equation will only cause more confusion for China’s tax authorities and companies’ over-stretched tax departments. It will be a busy year in China.

“While we hope the above measures can happen in 2016, there are also concerns that the rules and regulations to implement the above will not be clear, which is often the case in China,” says An Chang.

China has already issued a tax circular based on the BEPS principles, and it is expected that further updates will follow to fine-tune the jurisdiction’s approach to BEPS in 2016. The key concern for taxpayers is how well local tax authorities will understand, implement and enforce these national rules.

With the G20 presidency passing to China for 2016 (see Cunningham Column, page 3), the eyes of the international business community will be fixed on the Asian powerhouse even more firmly than before.

## Europe

Things are simpler – though far from simple – in Europe. National governments in this region in particular are performing a balancing act. As they try to walk the most optimal path between adoption of international best practices (and incoming transparency initiatives) and maintaining a competitive tax regime, the traditional European jurisdictions for locating holding or conduit companies may change.

“One key point to monitor within OECD and non-OECD jurisdictions alike in the wake of the OECD’s BEPS project will be whether the granularity inherent in jurisdiction-by-jurisdiction

implementation of (or decision not to implement) the outcomes of the BEPS project will in itself lead to the types of arbitrage or competition between tax systems which the BEPS project was intended to eradicate,” says Alex Jupp, counsel at Skadden, Arps, Slate, Meagher & Flom in the UK.

Cherry-picking of measures and inconsistent implementation will create more instances of the ‘mismatches’ the BEPS project was aimed at stamping out, as pointed out by Teijeiro and others.

“Only a consistent implementation of the above rules will ensure and allow a fairer, clearer and more certain legal system that will benefit all interested stakeholders,” agrees Filipa Correia of Valente Associati GEB Partners in Italy.

One unilateral anti-base erosion measure that taxpayers have been contending with for more than six months now is the UK diverted profits tax (DPT). With this model already in place, taxpayers in other countries are watching to see if similar legislation is contemplated elsewhere.

“I will be watching other countries’ adoption of taxes similar to the UK’s DPT,” says Tolin. “There is an open question of whether DPT will be eligible for the US foreign tax credit, but frankly I believe that question is largely academic; DPT looks more like a deterrent than a tax that will be actually paid by many taxpayers in the future.”

“But the proliferation of taxes similar to DPT will be an issue to watch as it relates to multinationals’ tax planning, and more generally to the status of treaties that might be violated by these taxes.”

Correia says she is also concerned about the amount of domestic room for manoeuvre in interpreting BEPS Action 1 recommendations.

“We are concerned with a potential increase of unilateral implementation of BEPS recommendations by the single countries, as well as any potentially divergent measures that might be implemented domestically on the digital economy,” says Correia. “The report on Action 1 (see page 24) leaves too much room for decision to countries.”

But in Europe, like in Latin America, taxpayer concerns for 2016 are not just prospective in nature. On top of incoming



EU taxpayers will be affected by initiatives at EU level, as well as BEPS

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changes, taxpayers need to grapple with domestic reforms handed down in the past two to three years.

In Europe, the number of tax reforms has largely outpaced legislative activity in other regions.

“Having studied the World Bank Group’s *Doing Business 2016* report, OECD high-income economies recorded more reforms in the area of ‘paying taxes’ than any other region,” says Mariana Vicente, who has performed tax planning lead roles for Odebrecht Agroindustrial, Sky, Dell and Boehringer Ingelheim.

“Most of them introduced or enhanced electronic filing and payment systems or reduced the tax burden for businesses.”

In Europe, Norway, Poland, Slovakia and Spain are examples of such countries that have implemented a number of reforms for taxpayers to contend with in the past year or so.

“Norway made starting a business easier by offering online government registration and online bank account registration, and it made paying taxes less costly for companies by reducing the corporate income tax rate,” says Vicente, who is joining Deloitte in Denmark from January. “Poland made paying taxes easier for companies by introducing an electronic system for filing and paying VAT and transport tax, while the Slovak Republic also introduced an electronic VAT system, as well as reducing the corporate tax rate.”

“Spain is another jurisdiction that has eased the compliance burden for businesses by modernising the online system for filing VAT returns,” adds Vicente.

In the UK, George Osborne, Chancellor of the Exchequer, will continue to develop his strategy to make the country a ‘jurisdiction of choice’ for multinationals in 2016. The UK, in particular, is a jurisdiction of interest to the extent that it has been at the forefront of calls for ‘fairer’ corporate taxation, while also fostering a business-friendly regime characterised by successive cuts in the corporate tax rate.

There may also be new entrants to the tax competition game in the form of jurisdictions such as Northern Ireland, which is gaining greater control over tax policy and is set to implement a highly competitive 12.5% headline corporate tax rate. Whether this proves to be enough to attract investment away from the likes of neighbouring (Republic of) Ireland, remains to be seen, but this will give taxpayers something to think about – particularly US-based companies that are looking to expand into Europe.

But despite tax competition remaining as a strong force in Europe, the uncertainty stemming from multilateral measures is an overriding factor, and is already proving detrimental to business growth.

“The uncertainties around Europe are, in my view, negatively influencing business decisions and major deals and transactions,” says Pieris Markou, partner at Deloitte Cyprus.

However, it is certainly not all doom and gloom. The BEPS project as a whole has a lot of positive connotations in some areas, particularly in dispute resolution – which will certainly be necessary, given the rash of disputes which will flare up once BEPS implementation into national legislation begins to gather pace – in conjunction with the re-emergence of alternative dispute resolution methods, which were largely ignored in Action 14 (see page 45).

“In many cases, at least in all those involving transfer pricing, we expect that disputes would be handled through MAPs rather than through judicial litigation,” says Luis Manuel Vinales of Garrigues–Taxand in Spain.

“We are rather optimistic about the attainment of a sound and improved dispute resolution mechanism, able to deal effectively with any disputes that we expect might increase,” says Correia.

“The solutions that clients need will most likely require the work of legal teams not only during a given litigation procedure but throughout all preliminary phases as well (that is, planning, designing, ensuring compliance, gathering, preparing, analysing data, monitoring developments and consequences that can derive from such changes),” she adds. “By focusing on compliance our clients would avoid further disputes.”

### Snakes and ladders

A number of Europe-wide initiatives will resurface in 2016 alongside the BEPS related concerns already outlined. While it is unlikely that these new mechanisms will actually come into force during 2016, taxpayers will need to keep a keen eye on any progress made on the financial transaction tax (FTT) and on reviving the common consolidated corporate tax base (CCCTB).

“The European Commission has also launched a public consultation to help identify the key measures for inclusion in the re-launch of the proposal for a CCCTB. The call for feedback comes as part of the implementation of the Commission’s Action Plan for Fair and Efficient Corporate Taxation which was presented in June this year,” says Vicente. “A wide range of views is sought from businesses, civil society and other stakeholders. The Commission intends to come forward with revised legislation next year.”

“The main focus of the CCCTB is on facilitating EU and third-country business, primarily those active in more than one member state within the EU,” explains Vicente. “In addition to creating a business-friendly environment by reducing the administrative burden, compliance costs and legal uncertainties for companies, the CCCTB has been presented as an effective tool against aggressive tax planning.”

Given failed attempts to get the CCCTB up-and-running in recent times, this is likely to be a ‘watch’ item for taxpayers in 2016, rather than anything that will need to be acted upon. One theme that is not merely a ‘watch’ item for 2016, however, is country-by-country reporting (CbCR).

“The [CbCR] requirements will affect a multinational as soon as one country adopts them, at least with respect to the master file and the CbC file,” says Tolin. “Will non-adopting countries be able to get their hands on the new reports through treaty information exchange mechanisms?”

Companies should already be working to update their systems to ease the transition into compliance with CbCR. While doing this, tax departments should also be aware of the EU Data Protection Regulation, which will be effective in a little over two years.

This is indicative of many of the 2016 trends identified by businesses as part of this look-ahead. Marrying compliance activity with a plethora of incoming legislative changes – at both national and international level – is surely going to keep taxpayers busy throughout 2016 and beyond. Staying on top of various changes, and ensuring other parts of the business are aware of these changes, will mean CFOs and tax heads must tread carefully to successfully navigate the ‘snakes and ladders’ landscape that has resulted from the collision of international tax transparency and national tax competition.