Tax Excellence Decoded

What the BEPS?

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Mr Sandison explored the BEPS Action Plan and highlighted key areas of focus, and discussed implications and strategies to manage these tax changes.

BEPS is a four-letter word that is sending many into a tailspin of fear and confusion. But is it the intended outcome of the Base Erosion and Profit Shifting initiative that people should be worrying about, or the unintended collateral damage that may be caused by the hurried implementation of an over-ambitious and naive attempt at saving the planet, or at least the revenue coffers of the fiscally-stretched Organisation for Economic Co-operation and Development (OECD) signatory nations?

To explore the meaning behind this seemingly simple and well-intentioned acronym, the Singapore Institute of Accredited Tax Professionals organised a BEPS technical session. Entitled “What the BEPS!?”, the session provided an overview and the fundamentals of this global development.

The session was facilitated by Accredited Tax Advisor (Income Tax) David Sandison, Managing Director, David Sandison & Co, who explained how the BEPS project evolved, where it is today and what it means for global business in general, and the Singapore economy in particular.

The participants were taken on a journey that started two decades ago in 1996, when the heads of the Group of Seven (G7) countries noted the trend that tax authorities did not seem to be getting their fair share of tax revenues as a result of various tax schemes crafted by seemingly grave-robbing “big businesses”.

OECD was tasked to look into this, and a report was published in 1998 which focused on tax havens and harmful preferential tax regimes. Fast forward a decade. The new BEPS plan was hatched following an ill-informed media frenzy on the back of the global financial crisis, which accused multinational corporations (MNCs) of not paying taxes proportionate to the revenues they earned in various (OECD) countries.

In this context, it was explained that revenues bear no direct correlation with profit, and that a company’s tax footprint is much bigger than the contribution it makes through corporate taxes on profit. A company’s total tax contribution will invariably include many other taxes. In a global survey by PwC UK, it was found that tax on profits only accounted for 15% of a typical big company’s tax contribution to the revenue coffers.

OECD's BEPS Action Plan
The objectives of the Action Plan on BEPS were thus put in context. The plan comprises 15 action plans which can broadly be categorised into three areas with the digital economy overarching the various action points in the plan. They are:

- **Coherence**

The plan aims to minimise instances of double non-taxation where companies do not pay taxes anywhere.

- **Substance**

The plan also addresses the need to prove substance when claiming to be the beneficial owner of income.

- **Transparency**

Part of the plan also entails a common transfer pricing approach covering documentation, methodologies and disclosure rules.

OECD reports
So far, various reports have been produced by the OECD which cover the following key areas:

- **Digital Economy**

One thing that is clear and duly recognised by OECD was that the digital economy pervades many aspects of BEPS. Tax challenges posed by the digital economy will be addressed in various action points in the BEPS Plan.

- **Hybrid mismatches**

A hybrid mismatch arrangement is one that offers a different tax outcome in the affected jurisdictions. A typical example would be a payment which is tax deductible in the paying country but is also not taxed in the hands of the recipient. The OECD's aim is to neutralise the benefit.

- **Countering harmful tax practices**

The OECD has embarked on an update of the 1998 report and finalised a review of the member countries' preferential regimes. There is intent to extend the participation in countering harmful tax practices to non-OECD countries towards the third quarter of 2015.

- **Preventing treaty abuse**

The OECD is intending to develop model treaty provisions and recommendations regarding the design of domestic rules to prevent the granting of treaty benefits in inappropriate circumstances. Tax treaties are not intended to generate double non-taxation.

One of the recommendations is to adopt the United States' model with regard to Limitation of Benefits (LoB). This is a main area of contention, as US' LoB is seen as outstandingly onerous and restrictive.

- **Transfer pricing aspects of intangibles**

One of the OECD's intentions is to develop a clear definition of intangibles. Being simple about it, isn't anything you own that you can make money out of but cannot kick, an intangible asset? The approach taken by the OECD appears to be heading in the direction of over-intellectualised paralysis by analysis.

One reasonable conclusion by OECD was that parties who have contributed to the development, enhancement, maintenance, protection and exploitation of the intellectual property (IP) ought to be appropriately remunerated. They soon got back to form though, by concluding that hard-to-value intangibles were, well, hard to value.

- **Transfer pricing documentation and country-by-country reporting (CbCR)**

Probably the most talked-about area, the CbCR is a three-tiered approach comprising a master file prepared by headquarters, a CbC report and a local file. This approach will provide tax authorities with a total picture of an MNC's operations, where its profits are and whether the allocation is justifiable. This puts a lot of information in places where there is scope for potential abuse. While the OECD's intention is to use this as a "risk assessment" tool, it remains to be seen if this is so. Implementation issues such as timing, confidentiality and consistency will need to be addressed.

- **Multilateral Instruments**

The OECD is considering the feasibility of using a multilateral instrument to implement BEPS measures and modify bilateral tax treaties. However, tax differs in every country. Challenges abound if a multilateral instrument is used as a basis to modify bilateral tax treaties. Herding cats will likely be more rewarding!

Overall impact of BEPS

It is the transfer pricing of intangibles and CbCR requirements that will potentially have the most immediate impact on global business. The first seems to follow some logic; the second may present an unintended outcome – misuse by the authorities who get hold of the information.

The action plan is ambitious and set to a very tight timetable. While the aim may seem to have some merit, it is sadly misguided in a number of ways:

1 It is based on a somewhat idealistic view of the global environment where the interests of different countries with different needs and cultures are aligned;

2 It assumes that all countries must form themselves in the image of OECD countries;

3 It is undoubtedly educating tax jurisdictions in the ways of the world and allowing them to become much more savvy – and thus potentially, more aggressive. This conflicts with the first assumption above;

4 It introduces little we haven't been discussing for years.

Singapore, though, should have little to worry about. It has amended Exchange of Information articles in its treaties and in April 2013, the Global Forum on Transparency and Exchange of Information for Tax Purposes affirmed through a peer review process that Singapore's EOI regime was in line with the EOI Standard. Other helpful factors are that:

– tax evasion is now a predicate offence for money laundering

– the IRAS makes residency difficult without commercial rationale

– tax incentives demand real substance

– it has transfer pricing laws that follow OECD's own

– its basic corporate rate is only 3% below that of the UK – so it is hardly a tax haven

While the weather is good in Singapore, it looks like it is going to get a lot hotter out there. It would be a wise move to get a good tax consultant – and some sunblock.

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About SIATP's Technical Discussions

SIATP's technical discussions have continually been very well received by accredited tax professionals. Unlike the run-of-mill Continuing Professional Educational courses which typically cover tax fundamentals, SIATP's interactive technical discussions are designed to cover tax issues that do not have clear-cut solutions or situations that may have different interpretations. Over time, these discussions contribute in boosting the overall tax standards in Singapore.

About Mr David Sandison

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With 30 years of tax experience, 23 of which have been in the Singapore and Southeast Asian tax and business environment, David has spent most of his time dealing with international advisory work across a whole spectrum of industries. Prior to setting up his own practice, David was a partner in one of the Big Four's Financial Services section of Tax where he was regularly involved in helping clients structure their venture capital, private equity and real estate fund projects, and worked closely with the firm's Mergers and Acquisitions, and Banking and Capital Markets teams in this regard. In addition, David also led the Tax training and technical departments.

David spent his formative years with Pricewaterhouse(Coopers) in London, and advanced his career with the firm in Melbourne, Australia before migrating to Singapore in 1991. A member of the Institute of Chartered Accountants in England & Wales, David is also an Accredited Tax Advisor (Income Tax), as well as a member of the Institute of Singapore Chartered Accountants.

This technical event commentary is written by SIATP's Assistant Director, Joanna Wong.