Base Erosion and Profit Shifting: Asia Pacific feels the impact

The Organisation for Economic Co-operation and Development (OECD) has unveiled their recommendations to tackle Base Erosion and Profit Shifting (BEPS). It's taken over two years from when the G20 finance ministers first called upon the OECD to develop an action plan to address BEPS issues.

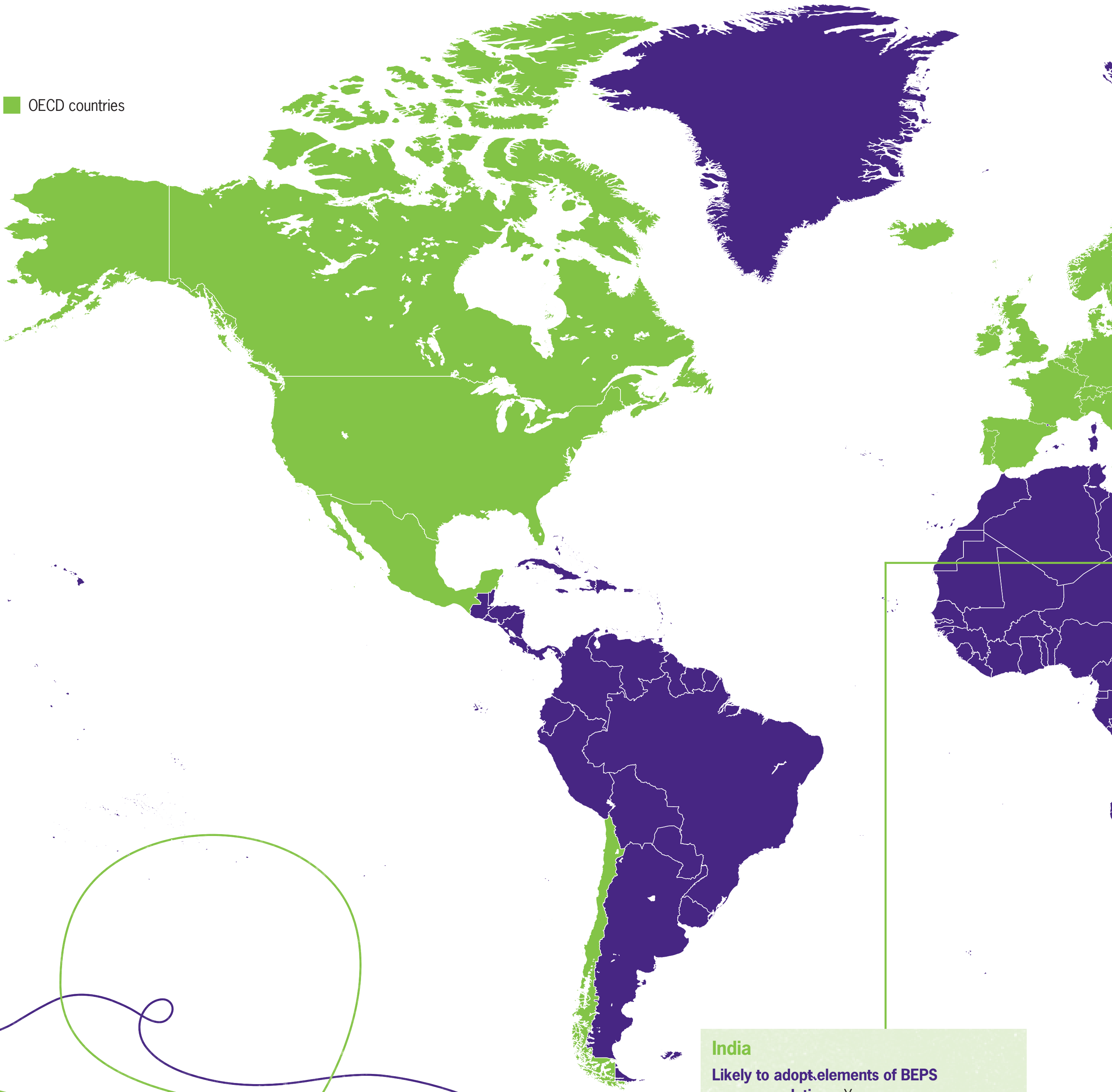
These measures were welcomed around the globe as evidenced in our research, which has shown that business leaders supported greater clarity as to what's acceptable and unacceptable tax planning, even if opportunities to lower tax liabilities were reduced.[1] But does the OECDs BEPS Action Plan result in a tax system that's fairer, more efficient and more transparent?

This guide provides an overview from a number of key countries within the region and highlights significant changes and insights for businesses operating in the Asia-Pacific region.

The region is one of huge diversity; culturally, geographically and economically. Japan is a world leader in the automotive and technology sectors and a member of the G7. Singapore is a global financial centre that rivals London and New York. And Australia and New Zealand are sometimes considered as a region in their own right. Interestingly, only four countries from this expansive region are members of the OECD. But, key economies such as China and India have indicated that they plan to adopt key elements of OECD recommendations into legislation.

[1] The Grant Thornton International Business Report (IBR), a survey of 2,580 businesses in 35 economies, found that three quarters of business leaders would pay more taxes in exchange for greater clarity from authorities on what is acceptable.

How will the region be affected and will the BEPS recommendations be adopted?

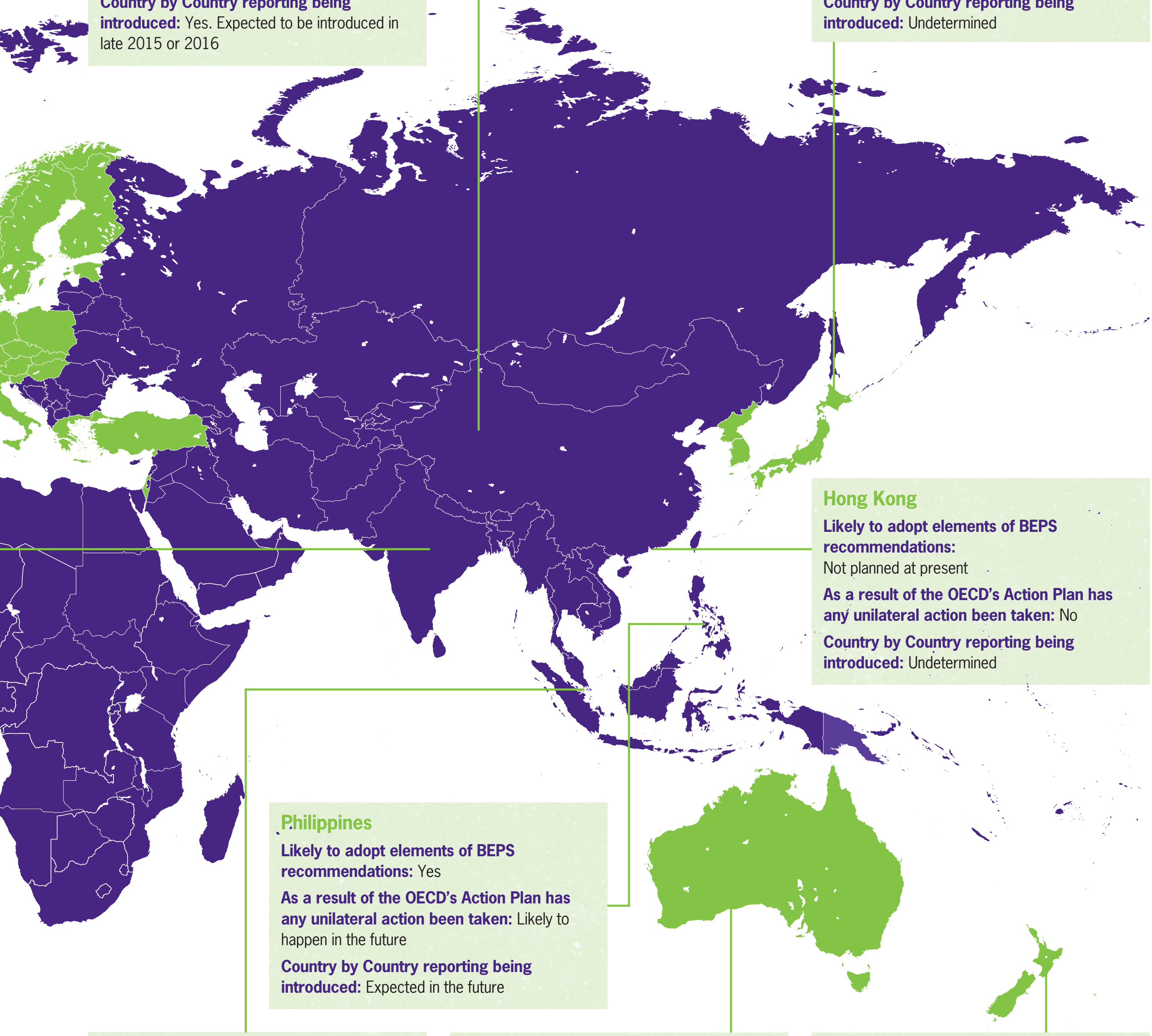


India

Likely to adopt elements of BEPS recommendations: Yes

As a result of the OECD's Action Plan has any unilateral action been taken: Likely to happen in the future

Country by Country reporting being introduced: Yes. Date of implementation unknown at present



China

Likely to adopt elements of BEPS recommendations: Yes

As a result of the OECD's Action Plan has any unilateral action been taken: Yes

Country by Country reporting being introduced: Yes. Expected to be introduced in late 2015 or 2016

Japan

Likely to adopt elements of BEPS recommendations: Yes

As a result of the OECD's Action Plan has any unilateral action been taken: Yes

Country by Country reporting being introduced: Undetermined

Hong Kong

Likely to adopt elements of BEPS recommendations:
Not planned at present

As a result of the OECD's Action Plan has any unilateral action been taken: No

Country by Country reporting being introduced: Undetermined

Philippines

Likely to adopt elements of BEPS recommendations: Yes

As a result of the OECD's Action Plan has any unilateral action been taken: Likely to happen in the future

Country by Country reporting being introduced: Expected in the future

Singapore

Likely to adopt elements of BEPS recommendations: Yes

As a result of the OECD's Action Plan has any unilateral action been taken: No

Country by Country reporting being introduced: Expected in the future

Australia

Likely to adopt elements of BEPS recommendations: Yes

As a result of the OECD's Action Plan has any unilateral action been taken: Yes

Country by Country reporting being introduced: Yes. 1 January 2016

New Zealand

Likely to adopt elements of BEPS recommendations: Yes

As a result of the OECD's Action Plan has any unilateral action been taken: No, a policy response is still being considered

Country by Country reporting being introduced: Yes. Expected to be introduced but no dates set

What effect will BEPS have to your daily business operations?

Businesses hoped the BEPS recommendations would provide the clarity and peace of mind required to satisfy stakeholders that they are 'paying their fair share of taxes'. However, in reality businesses may face a greater risk of double taxation. This could be down to timing differences in the implementation of BEPS actions, conflicting adaption of the measures and countries taking unilateral action. There is a genuine concern that dispute resolution has not been adequately addressed in Action 14 recommendations.

For countries that will implement BEPS, how likely is it that all elements will be imported into local legislation?

As many of the actions are merely recommendations, countries can effectively pick and choose the elements to enact or not enact. Dealing with variations in how the 15 actions are interpreted and implemented across the region and globe will undoubtedly cause headaches. To add to this uncertainty many businesses have operations in countries that will not follow or adopt BEPS requirements.

You need to review your businesses operations to ensure that all elements are compliant with local legislation (both current and tabled) in the countries where you operate. For multinationals, give consideration to restructuring certain aspects of your business, reorganisation of your business or operating model and reviewing intercompany transactions and financing arrangements. Other possible areas to consider would be permanent establishment rules and debt financing.

New Zealand businesses, irrespective of size, should review their international operations in light of BEPS recommendations. Amendments to transfer pricing documentation and mandatory disclosures are anticipated for larger businesses but may not be limited to this.

All international transactions and policies will need to be reviewed. Changes to debt funding and permanent establishment rules are examples of changes that could affect a large number of businesses even where they are not engaged in complex international tax planning.

China is revaluating its transfer pricing rules. Almost all the core BEPS initiatives and concepts have been incorporated, according to the latest official draft rules released for public consultation. These new rules will be applicable for all businesses irrespective of turnover, whilst businesses with a turnover greater than RMB 5 billion (approximately the equivalent to the BEPS threshold of €750 million) will be required to incorporate Country by Country (CbC) filing as part of their annual tax return filings.

All of this, in conjunction with CbC reporting (for those impacted), is likely to represent a significant additional administrative and compliance burden as current information systems may not be designed to provide what's required. Although the OECD have stressed that CbC reporting is purely designed as a risk assessment tool for tax authorities, there are concerns that this information could increase the risk of challenge by a tax authority.

For others there is a far greater concern that sensitive commercial data could become public. This could be through direct publication by the tax authority or from a cyber-security breach. It's currently unclear how governments plan to address this.

Australia has moved quickly to enact transfer pricing legislation that directly incorporates the OECD's transfer pricing guidelines. Draft legislation has also been released on new reporting standards for transfer pricing documentation and CbC reporting. These are the first tangible impacts in Australia flowing from the BEPS project. The proposed new reporting standards will affect many Australian resident companies irrespective of size, with larger multinationals and their Australian affiliates being required to file an annual statement to the Australian tax office.

Foreign companies with an Australian permanent establishment that has annual global revenues of over A$1 billion will also be impacted by these proposed changes. These entities will be required to file an annual statement covering one or more of the following:

- **CbC report** – includes the following information for each country where the multinational operates: revenue, profit (loss) before income tax, income tax paid, income tax accrued, stated capital, accumulated earnings, tangible assets, number of employees and main business activity
- **Master file** – an overview of the multinational's global business, its organisational structure and its transfer pricing policies
- **Local country file** – contains detailed information about the local taxpayer's operations and intercompany transactions.

The proposals also seek to double the penalties imposed on 'significant global entities' (members of a multinational group with annual global income of A$1 billion or more) that enter into tax avoidance or profit-shifting schemes.

Implemented legislation requires key information relating to a company's tax affairs (where their turnover is greater than A$100 million) to be disclosed to the Australian Tax Office (ATO). The ATO will publish this information (total income, taxable income and tax payable in respect of impacted businesses) on their website.

When will your business be impacted by BEPS?

The answer depends on where your business operates, but BEPS is likely to be affecting your business right now. You should be thinking about how this new tax environment affects businesses operations. Following a BEPS compliance review of your operating structure, you may need to make substantial changes and implementation may be lengthy.

India is committed to adopt Action 13. Businesses with a turnover greater than €750 million will be impacted next year when the CbC reporting requirements kick in. BEPS will also impact businesses with international operations that are being held through beneficial treaty regimes and where value chains are not aligned to the businesses functions.

The G20 countries, including countries outside the OECD such as India and China, have committed to introducing CbC reporting for large groups. This will include a central master file and local transfer pricing reports. Of the non-OECD G20 countries, China in particular has been an active contributor to the BEPS Action Plan and is expected to codify a majority of the BEPS concepts in its new domestic transfer pricing legislation.[2] Other countries in the region are expected to follow China's lead, making notable steps forward to internationally harmonise tax rules. With regards to other BEPS measures non-OECD countries are likely to pick and choose elements rather than enacting the recommendations in their entirety. Your business will be under more pressure to keep up to date with fast changing tax legislation across the globe.

Following the current public consultation period in **China**, the law is expected to be finalised and released by the end of 2015 or early 2016. This will pave the way for BEPS concepts to be implemented. Chinese businesses with international operations are affected by BEPS now.

[2] Draft legislation was released in China for public consultation on 16 October 2015 with a finalised version expected to be announced by the end of 2015 or early 2016. While changes are possible, all the fundamental BEPS measures as reflected in the public consultation draft will probably remain intact.

In **Australia**, the proposed new rules apply for income years starting on or after 1 January 2016. Annual statements will need to be sent to the ATO within 12 months of a business' year end.

Under proposed legislation, companies will face increased penalties for entering into schemes without a 'reasonably arguable position', if the dominant purpose is to reduce tax.

The compliance burden for Australian companies will increase as existing transfer pricing compliance will remain in addition to the new annual statement. Companies will still be required to maintain Australian transfer pricing documentation in order to establish a reasonably arguable position and be afforded access to penalty relief.

Although the **Hong Kong** Inland Revenue Department are currently not proposing to implement the BEPS concepts into local legislation, if your business has international operations you are likely to be affected by BEPS now.

Are there any specific industries that will be impacted more?

BEPS affects all industries, but some will face a greater impact than others.

Globally banking and insurance is likely to be affected substantially by the outcome of Action 2 (hybrid mismatches) and Action 4 (interest deductions). While the digital sector, including technology and e-commerce, will be particularly affected by many of the actions set out in Action 1 on the digital economy.

The perception of tax avoidance of industries in certain jurisdictions will also colour how the BEPS measures are introduced around the globe.

In **India**, software, pharmaceuticals and automotive industries which have significant outbound operations will possibly be affected more so.

Businesses operating outside **New Zealand** have already started to feel the impact and are revisiting their global strategies. For businesses with operations in New Zealand the impact of BEPS is expected to be imported into domestic legislation on a piecemeal basis over the next few years.

The legislative process is expected to be measured. It will need to pass through the normal channels that require policy consideration, public consultation and compliance cost analysis.

Regardless of the complexity of the international tax planning, many businesses that have international dealings will be conscious of having good practices for their internal tax governance. This will include compliance with recently issued **Singapore** transfer pricing guidelines and adherence to revenue authority statements in relation to BEPS. How Singapore responds to BEPS will be of interest, as it's a prominent jurisdiction for hosting and as a hub for commercial operations.

Although no specific industry in **Singapore** is expected to see a greater impact, companies that have been granted tax incentives (that result in zero or low tax payable) in Singapore may be more susceptible to BEPS challenges in the country where they are headquartered.

In **Australia** most of the activity regarding BEPS and multinational tax avoidance has been centred on the technology, pharmaceuticals, life sciences and mining industries. There has also been a Senate Committee inquiry into corporate tax avoidance where companies from these industries were probed on profit-shifting and transfer pricing policies. It is expected that these industries will be the main focus of the ATO's attention.

How can you prepare your business?

BEPS has received considerable attention over the past few years, to the extent that some businesses may have become detached from the process. But it's now that you should be critically appraising your current corporate structures to make sure they are fit for purpose. Businesses face a number of issues including:

- divergences in domestic legislation in the countries they operate
- archaic tax authority dispute resolution mechanisms
- an eagerness from tax authorities around the globe to ensure they collect their 'fair share' of tax.

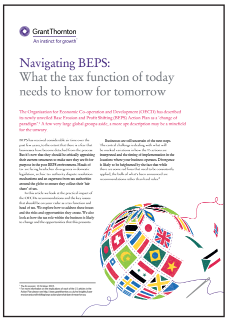
The key is to have real substance. Businesses should take note and understand the underlying principles of BEPS reform. You need to adopt tax governance and risk management processes that consider potential reforms in common areas of transfer pricing and determination of permanent establishments, particularly if you're involved in e-commerce.

You need to document your operations in each tax jurisdiction and include the economic and operational decisions made to justify your corporate structure. You must also ensure transfer pricing documentation is kept on file including necessary preparation of 'reasonably arguable position' papers for arrangements that may fall under new rules.

In addition, companies should 'pressure test' their current operating structure and consider whether their commercial or financial arrangements could be considered profit shifting or tax avoidance schemes.

New Zealand businesses should review their global operations; it's very likely that there will be divergences across the region and globe. Implementation strategies will be required to address the changes which will affect global operations. Strategies should cover ways to avoid or minimise potential double taxation and disputes as well as timing differences.

For the first time, multinationals operating in **Australia** will need to provide detailed information as part of their annual compliance reporting to the ATO. It allows the ATO an unprecedented level of transparency into the financial and commercial operations of multinationals. The ATO will be able to better target transfer pricing risks and allocate its resources accordingly. Along with increased penalty regimes, this is also likely to impact board level governance in relation to tax risk management.


Grant Thornton
An instinct for growth
Navigating BEPS:
What the tax function of today needs to know for tomorrow

In our publication 'What the tax function of today needs to know for tomorrow' we highlight five actions that will help your business to navigate BEPS related legislative changes:

1. The BEPS Action Plan indicates that some operational restructuring and adjustments to transfer pricing may be required by businesses. But given the current uncertainty it would be beneficial to model the different outcomes and develop clear contingency plans rather than taking hasty action now.
2. We believe that interest rate deduction is one of the grey areas where your tax teams should model the implications of different levels of deductions, and consider how to deal with the varying outcomes. However, it would be unwise to make wholesale changes before you know what fixed ratio each of the legislatures settles on.
3. It's vital that any risks are identified in how CbC disclosures will be assessed in each jurisdiction and proactively prepare to defend potential threats.
4. Tax functions should provide the board and business teams with regular communications about how the BEPS recommendations will affect their strategy and operations.
5. Uncertainty over the final direction of BEPS and the wider tax regime will continue. But substance can't be changed overnight. So it's important to start planning any necessary relocation or restructuring as soon as you can.

If you would like to discuss any of the issues raised, then please speak to your usual Grant Thornton contact or one of the contacts listed below.

Australia
Jason Casas
E jason.casas@au.gt.com

China
Richard Bao
E richard.bao@cn.gt.com

Hong Kong
William Chan
E william.chan@cn.gt.com

India
Arun Chhabra
E arun.chhabra@in.gt.com

Japan
Hideharu Tanaka
E hideharu.tanaka@jp.gt.com

New Zealand
Greg Thompson
E greg.thompson@nz.gt.com

Philippines
Eleanor Lucas Roque
E lea.roque@ph.gt.com

Singapore
Peter Godber
E peter.godber@sg.gt.com

Grant Thornton
An instinct for growth™

www.grantthornton.global

Grant Thornton International Ltd is a company limited by guarantee incorporated in England and Wales.
Registered number: 05523714
Registered office: Grant Thornton House, 22 Melton Street, Euston Square, London NW1 2EP