

Practical Consequences of the OECD/G20 – Anti-BEPS Initiative

A Business Study by Baker & McKenzie – Tax Practice Group





Editorial for the BEPS Study by Baker & McKenzie

For international businesses, the *Anti-Base Erosion and Profit Shifting* (BEPS-) Initiative of the *Organisation for Economic Co-operation and Development* (OECD), the *G20* and the *European Union* (EU) constitutes the most strident change in tax policy since the agreement on the OECD model treaty in 1963. The proponents of the initiative regard it as necessary in order to fight aggressive, yet legal, tax avoidance.

The thought work contained in 15 action reports published by the OECD on October 5, 2015 is already used by numerous tax authorities in their tax practice and enforcement. In view of this background, there is no doubt that the BEPS Initiative has started to lead to an increase in tax allocation conflicts between individual countries. Once the actual proposed measures of the OECD action reports and the EU commission has transformed into binding legal rules, the allocation conflicts will increase at the expense of businesses. Nonetheless, both politics and the media continue in their support of the Anti-BEPS Initiative.

With this situation in mind, the tax practice group of Baker & McKenzie reached out to give a voice to the in-house tax experts of the businesses most affected by the Anti-BEPS Initiative. During the period November 2015 through February 2016, in-house tax experts of international and domestic businesses were interviewed as to their assessment of the practical impacts of the Anti-BEPS Measures. The interviews took place as part of online contacts with mainly German enterprises with international activities. The results should supply decision-makers in enterprises, politics and media with substantial input for their consideration.

The following pages show the results of the interviews.
We wish you an inspiring lecture!

Contents

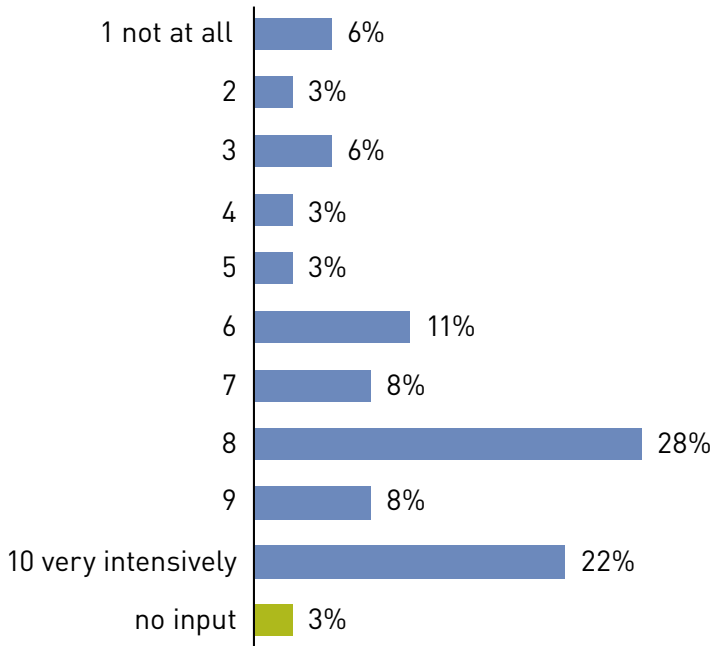
A	Importance of BEPS Initiative in your enterprise	5
B	Impact of the BEPS Initiative on enterprise processes	9
C	Experience with current tax field audits	11
D	Practical impact of the BEPS Initiative on your enterprise	14
E	Impact of BEPS Initiative on growth and competitiveness of your enterprise	20
F	EU law aspects of BEPS	24
G	Tax policy aspects of Anti-BEPS Measures	27
H	Impact of BEPS Initiative on tax department	31
I	Questions regarding the respondents	33
	Contacts	36



A

Importance of
BEPS Initiative
in your enterprise

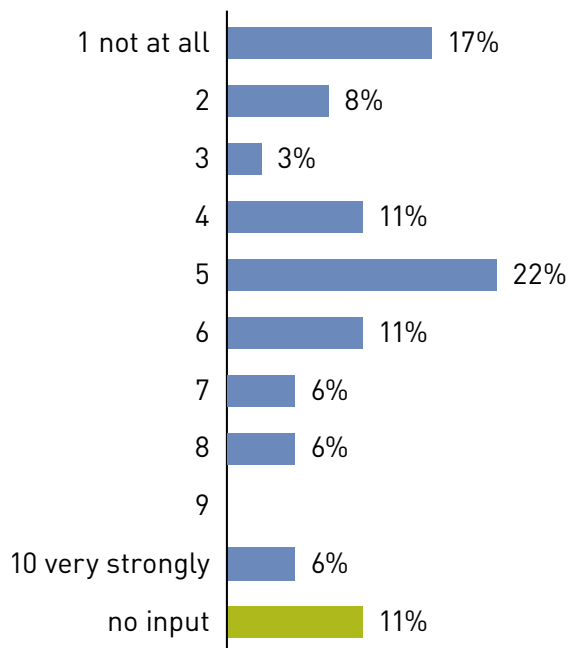
To what extent does the tax department in your enterprise already investigate the (possible) impact of the BEPS Initiative?



The tax departments are familiar with the topic

- ▶ Almost 60% of the tax departments take an intensive or very intensive interest in the impact of the BEPS Initiative. 22% of all tax departments have studied BEPS intensively.
- ▶ Only 15% have taken a slight or no interest in the BEPS Measures.

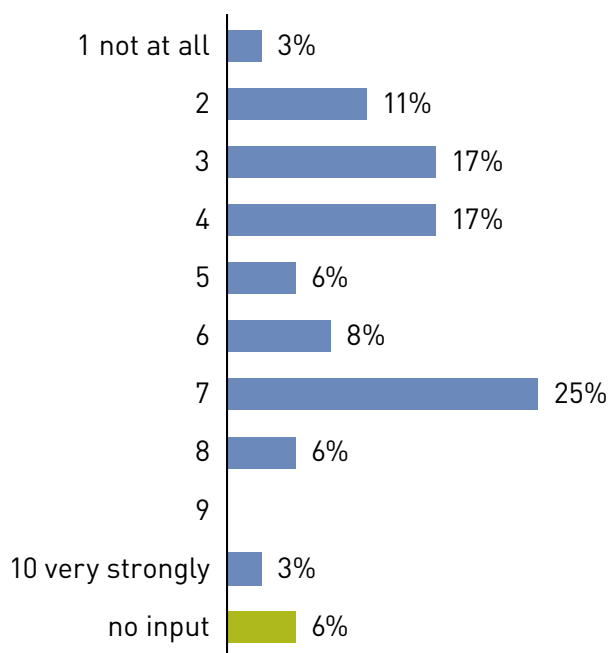
To what extent does board level management of your enterprise take an interest in the (possible) impact of the BEPS Initiative?



Management levels need to show more interest

- ▶ In contrast to the tax departments, the topic does not appear to have arrived on the horizon of management. Only 12% of respondents report a strong or very strong interest in BEPS on the part of management.
- ▶ Nearly half of the tax experts experience no more than a half-hearted interest on the part of board level management with the BEPS Initiative.
- ▶ For 28% of respondents, management has shown either very little or no interest in BEPS and its practical consequences.

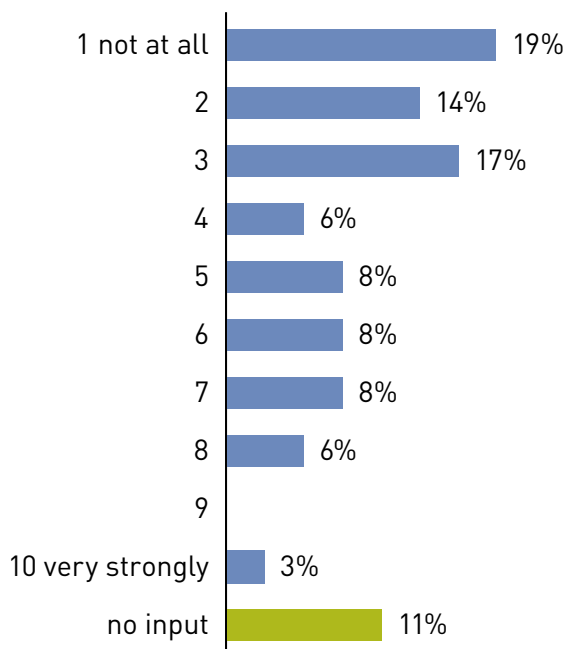
Does the BEPS Initiative result in a closer coordination with other areas of the enterprise (e. g. Finance/Controlling, Investor Relations, PR/Communication)?



There are only some cases, where BEPS has an influence on the cooperation within enterprises

- ▶ Nearly one third of respondents does not experience a (noticeable) strengthening of the collaboration with other areas of the enterprise.
- ▶ On the other hand, more than one third of representatives do report a clear or even strong to very strong increase in cooperation transcending individual departments.

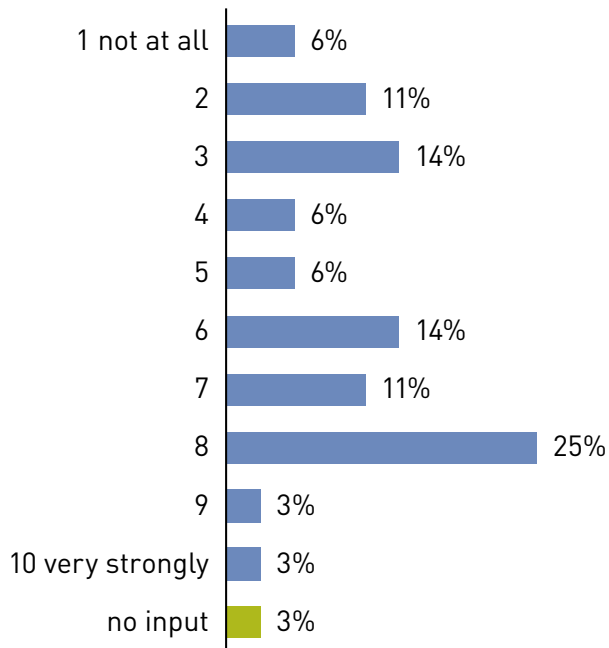
To what extent has direct cooperation between the tax department and the board/management level increased since the beginning of the BEPS discussion?



In most cases, BEPS has no impact on the communication with management

- ▶ For 50% of respondents, BEPS has very little or no impact on communication with the management level of the enterprise.
- ▶ When comparing the low level of interest shown by management in Anti-BEPS matters (above), there is even less communication with management on Anti-BEPS matters.
- ▶ Only 9% believe that communication will increase strongly or even very strongly.

To what extent does the BEPS Initiative already have an impact on ongoing tax planning and tax structuring in your enterprise?



BEPS will influence tax planning and tax structuring in the enterprise

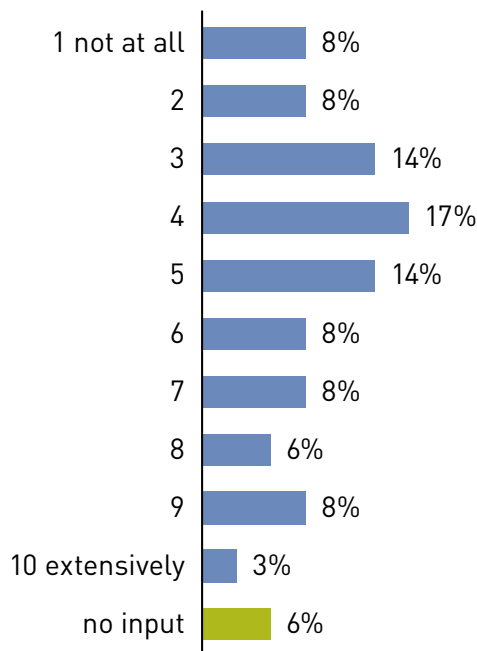
- ▶ 31% of respondents are of the opinion that BEPS will have a strong or very strong influence on tax planning and structuring.
- ▶ 38% of respondents see a moderate, more or less pronounced impact on their own tax planning and structuring.
- ▶ Another 31% of the tax experts expect no or very little impact.



B

Impact of the
BEPS Initiative
on enterprise
processes

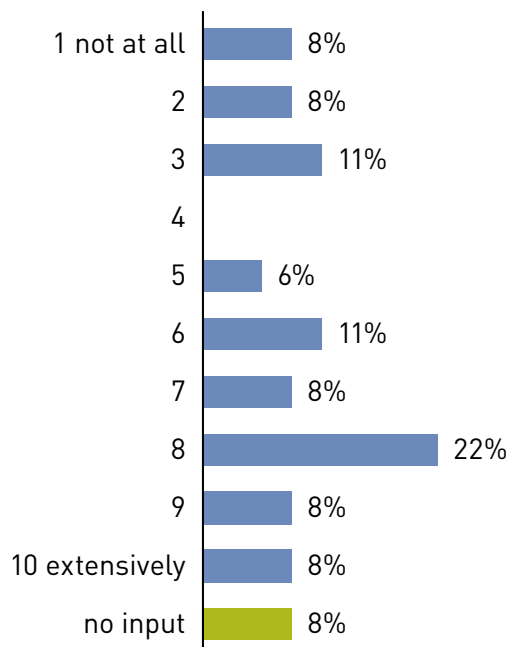
To what extent do the business compliance processes already reflect the requirements imposed by BEPS (e. g. BEPS Health-Check in acquisitions)?



Considerable backlog in compliance processes

- ▶ Very few businesses have adjusted their compliance processes extensively or adequately to the BEPS requirements. Only 17% of the businesses interviewed are prepared.
- ▶ Approx. 39% of respondents estimate their enterprise to be in the (lower) middle in terms of preparation.
- ▶ For another 30%, the processes have not been adjusted at all or hardly.

Has your enterprise already developed processes for the purpose of addressing future requirements of the country-by-country reporting?



For the purpose of country-by-country reporting the transformation is more advanced than in the compliance processes

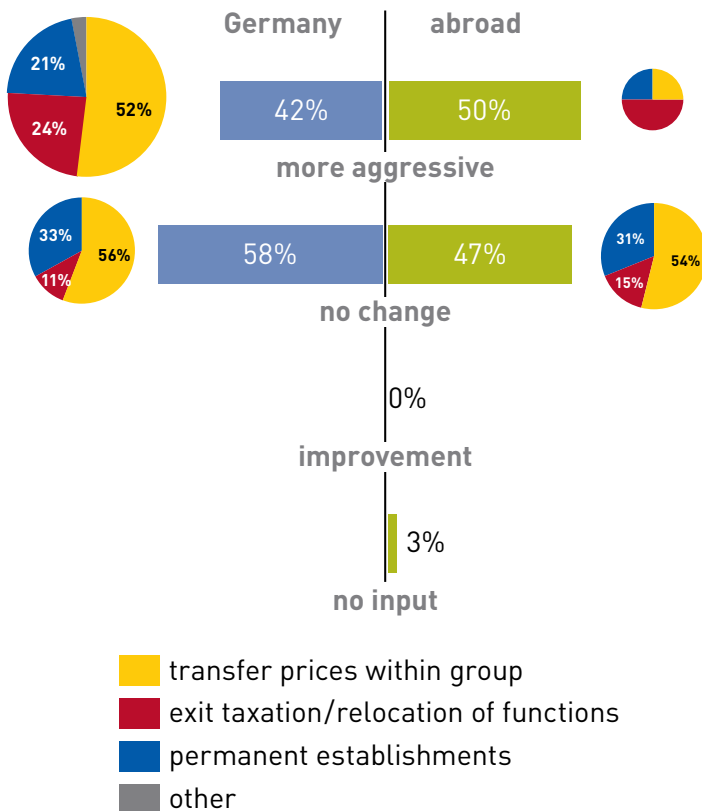
- ▶ In contrast to the compliance processes enterprises are more advanced in the country-by-country reporting. Almost 40% of respondents have already developed extensive or comprehensive processes.
- ▶ 27% of the enterprises have not or hardly started with preparations. The other businesses are engaged in the development of processes.



C

Experience with
current tax field
audits

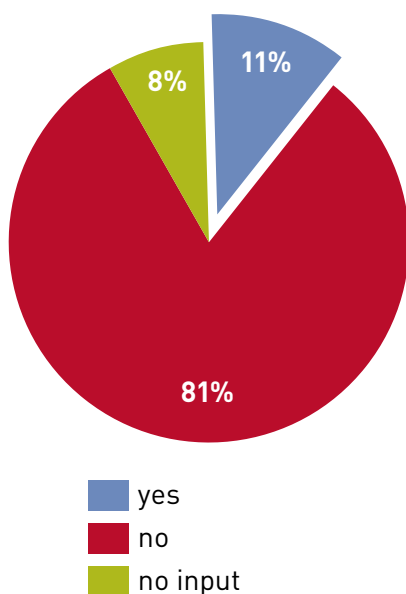
Have you, since the beginning of the BEPS Initiative, noticed a change in the approach of auditors in tax field audits in Germany or abroad? If so, in which areas?



No improvement in sight

- None of the respondents has experienced a change in the methodologies of tax field auditors, whether domestically or abroad.
- Approx. 60% of respondents did not discern any change in the audit approaches in Germany and 47% did not notice a change of approaches abroad. Both domestically and abroad it is mainly the group internal transfer prices which are audited.
- A tougher approach in tax field audits in Germany is witnessed by 42% of the respondents and abroad by even 50%.
- In Germany, this concerns in particular group internal transfer prices, Abroad, the focus appears to be mainly on exit taxation and relocation of functions.

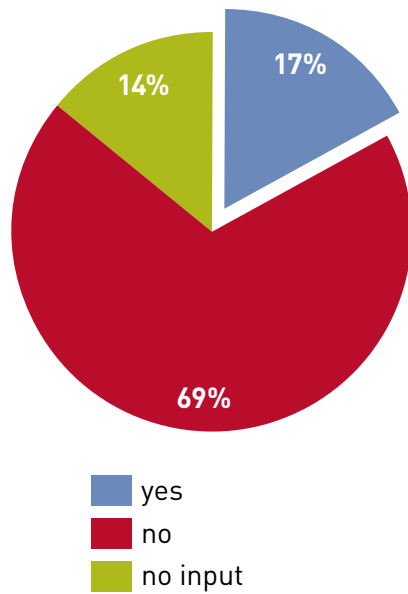
Have you, since the beginning of the BEPS discussion, observed an increase in unspecified audit enquiries (“Fishing Expeditions”)?



No increase of “Fishing Expeditions”

- 81% of respondents have not observed an increase in non-specific audit enquiries (“Fishing Expeditions”).
- An increase of “Fishing Expeditions” was only observed in isolated cases (11%).

Since the beginning of the BEPS discussion, have you observed an increase in cross-border information exchanges between tax administrations?



Every sixth enterprise did observe an increase in cross-border information exchanges

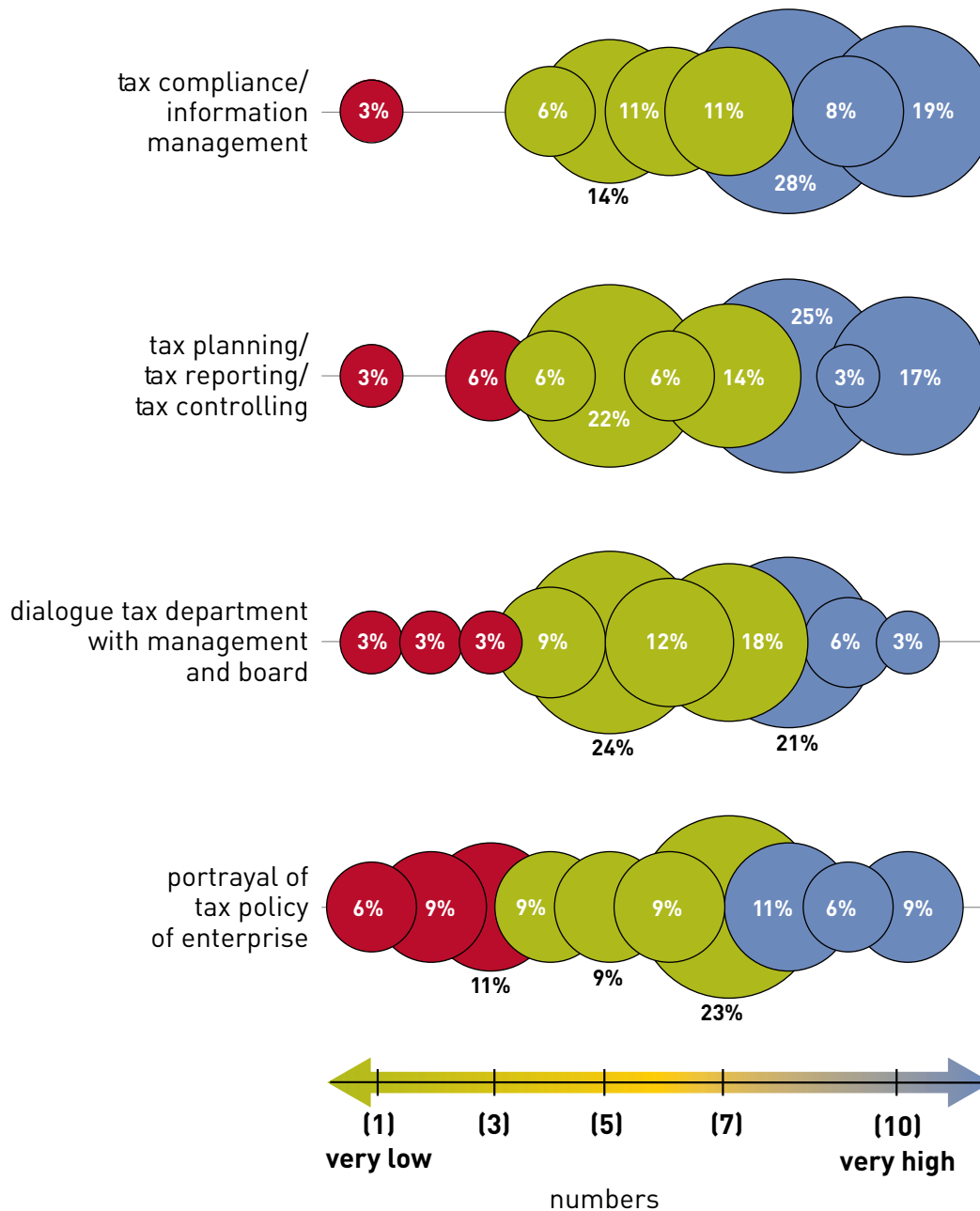
- › 17% of respondents observed an intensified cross-border information exchange.
- › More than two thirds of respondents did not observe such increase.



D

Practical impact of
the BEPS Initiative
on your enterprise

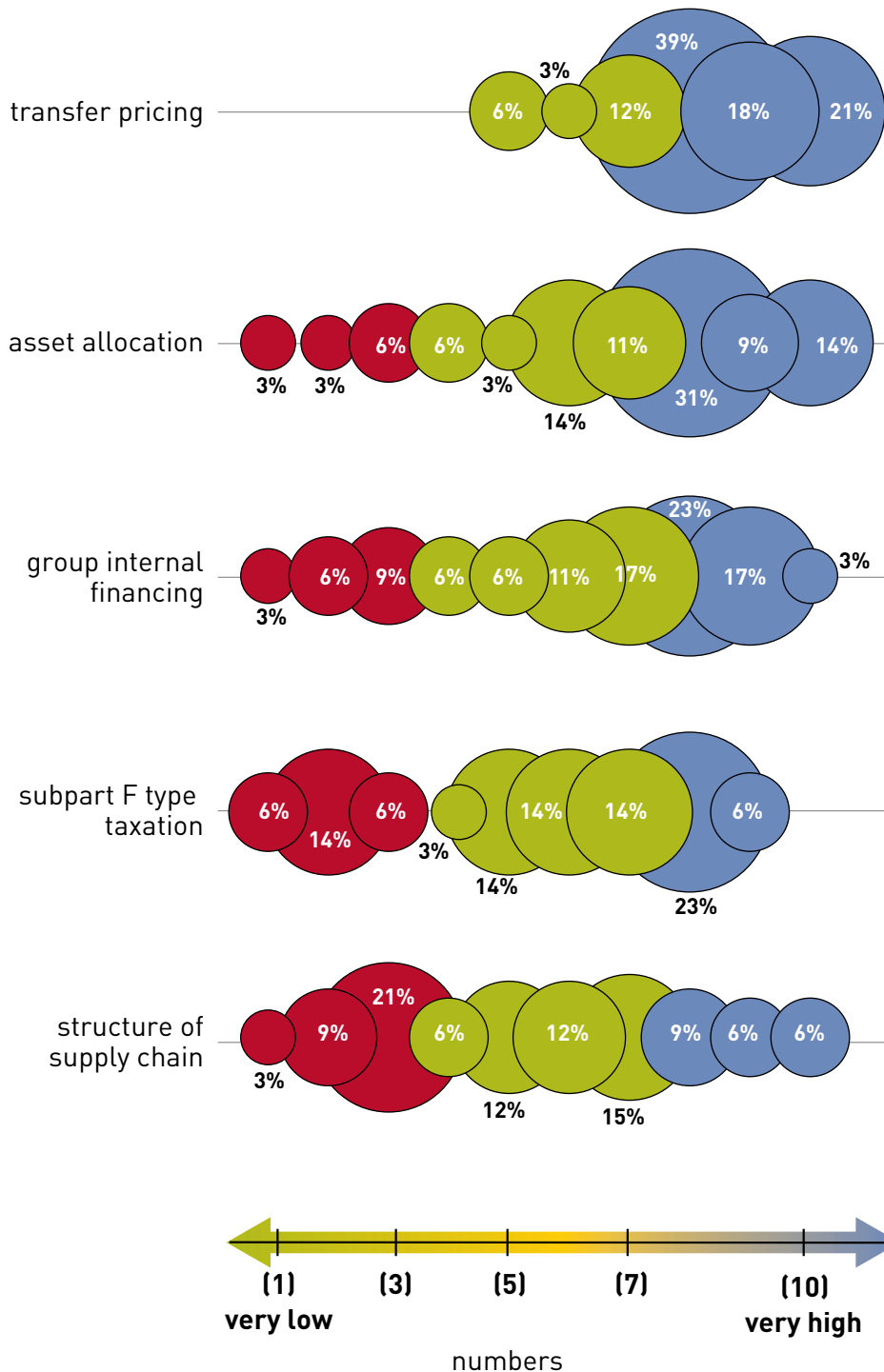
Where do you see the priorities in preparing your enterprise for BEPS? The priority is in the area ...



The priority is in tax compliance and information management

- ▶ 55% of respondents accord high or highest priority to tax compliance and information management when preparing their enterprise for BEPS.
- ▶ Nearly half of the tax experts accord a high or very high priority to tax planning and tax reporting/controlling.
- ▶ The dialogue of the tax department with management is accorded an average priority only.
- ▶ The communication with the public regarding the portrayal of tax policy is rather more important for the respondents. It is interesting that there is also a quarter of respondents who regard the portrayal of the tax policy as unimportant.

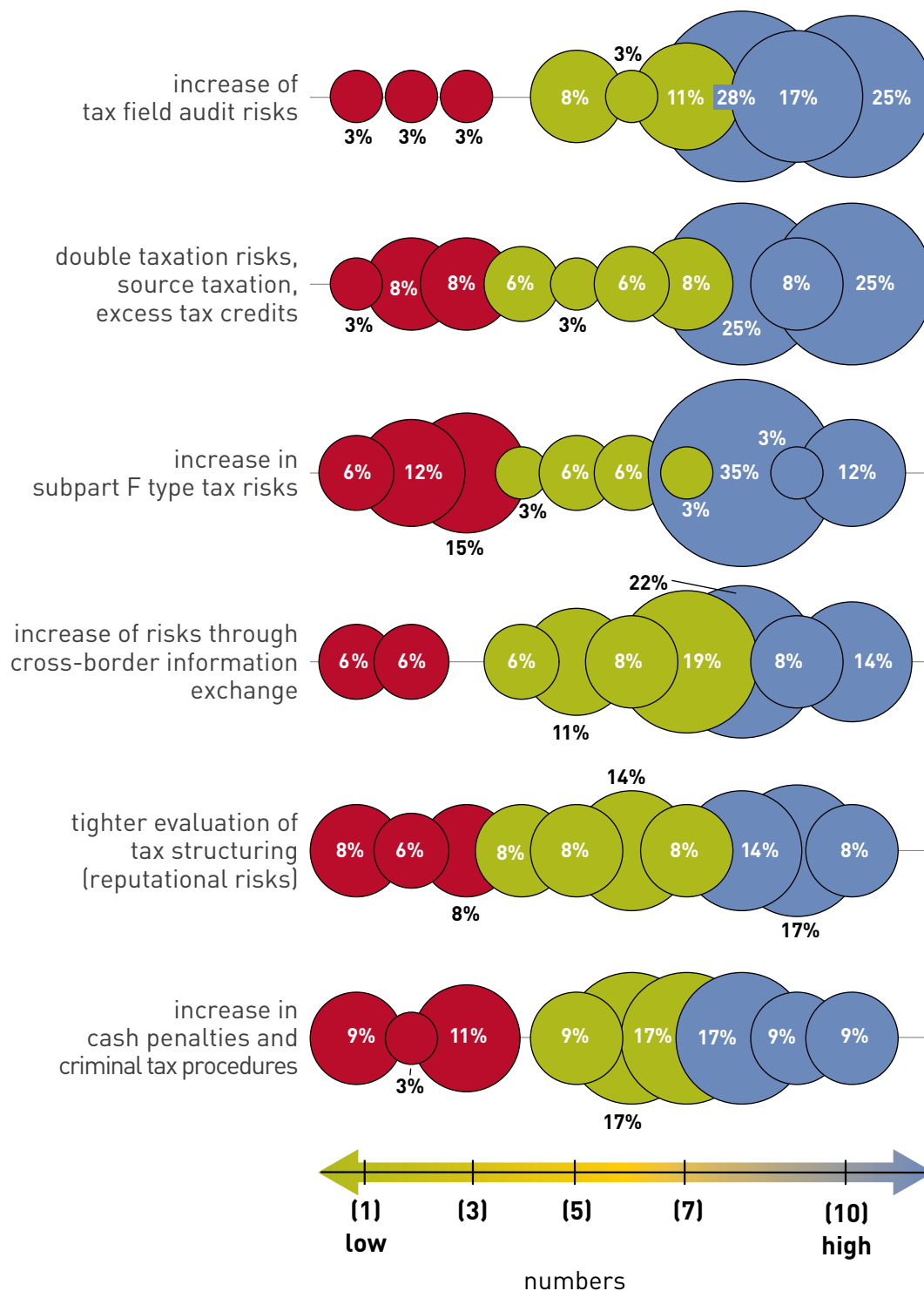
Which are the areas where you expect the greatest practical impact or changes because of BEPS? The impact is greatest in the area of ...



Transfer pricing in focus

- › 4/5 of enterprise representatives expect the greatest practical impact or changes through the BEPS Initiative in transfer pricing. There was not a single person who accorded a low value to this point.
- › In addition, about half of the respondents expect a strong or very strong impact on the tax allocation of assets.
- › Less impacted are financing structures and subpart F type taxation and, least of all, the structure of supply chains.

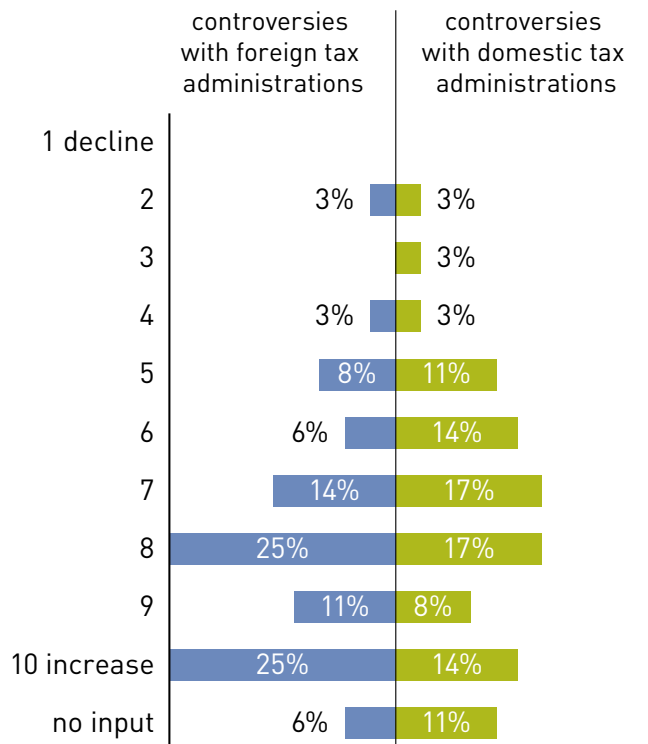
Which risks do you expect for your own enterprise? The risk is with ...



Risks are all assessed as very high

- ▶ The risks as shown on the left of the chart are all assessed as rather high when compared to the practical impact and priorities in preparation.
- ▶ There is a very high expectation of the probability of an increase in tax field audit risks, two thirds of the respondents expect this risk.
- ▶ Almost half of the respondents point to risks from double taxation/source taxation/excess foreign tax credits.
- ▶ There is a deviation when judging the risk from subpart F type taxation. The tax departments either have a high or a rather lower expectation of risk.
- ▶ Every third respondent recognises high or very high risks of tax criminal prosecution and sanctioning and the danger of reputational damages.

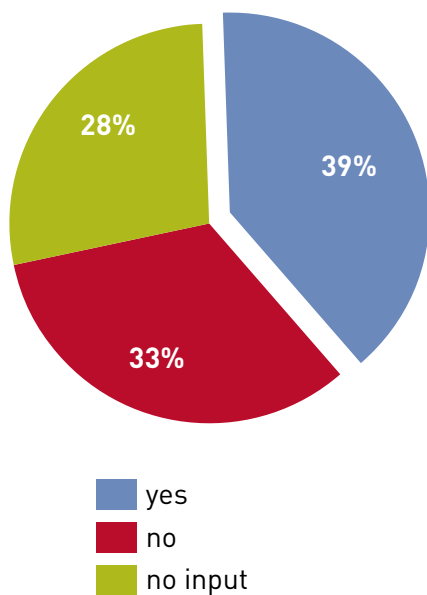
What impact do you expect the BEPS Initiative to have on your relationship with domestic and foreign tax authorities? Will tax controversies rather increase or rather decrease?



There will be controversies both domestically and abroad

- ▶ Three out of four respondents expect an increase of controversies with foreign tax authorities.
- ▶ More than half of enterprise representatives expect increased conflicts with domestic tax administrations.
- ▶ There are very few who believe that domestic and foreign controversies will decline.

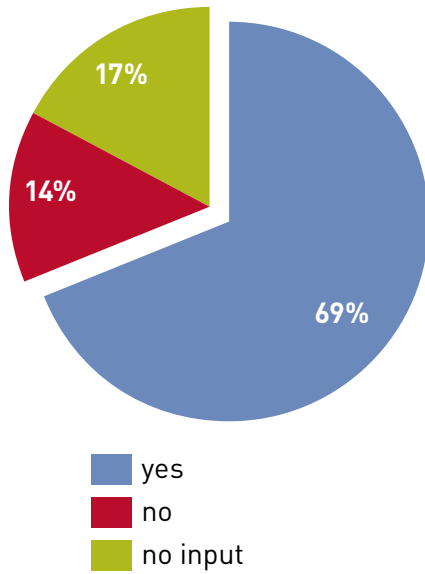
Will your enterprise in future make more use of Advance Pricing Agreements in order to limit double taxation risks?



Advance Pricing Agreements are only desirable for some

- ▶ Almost 40% of the respondents are already certain that they will make more use of Advance Pricing Agreements in order to limit double taxation risks.
- ▶ Nearly 2/3 of company representatives see no need for additional Advance Pricing Agreements or are not certain.

In future, will your enterprise make more use of competent authority proceedings in order to limit (the threat of) double taxation?



Competent authority proceedings are regarded as useful

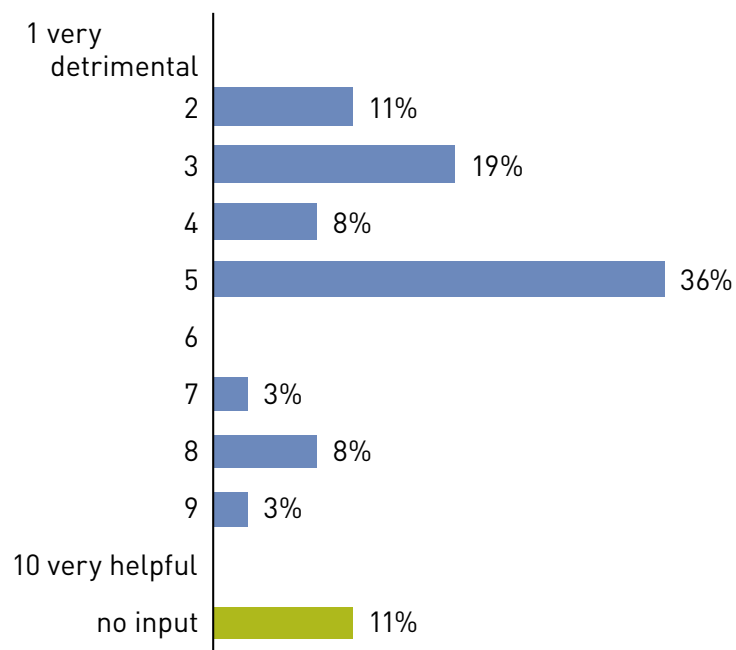
- More than two thirds of the respondents will access competent authority proceedings in order to limit (the threat of) double taxation.
- 14% see no necessity to employ these proceedings more often.



E

Impact of
BEPS Initiative
on growth and
competitiveness
of your enterprise

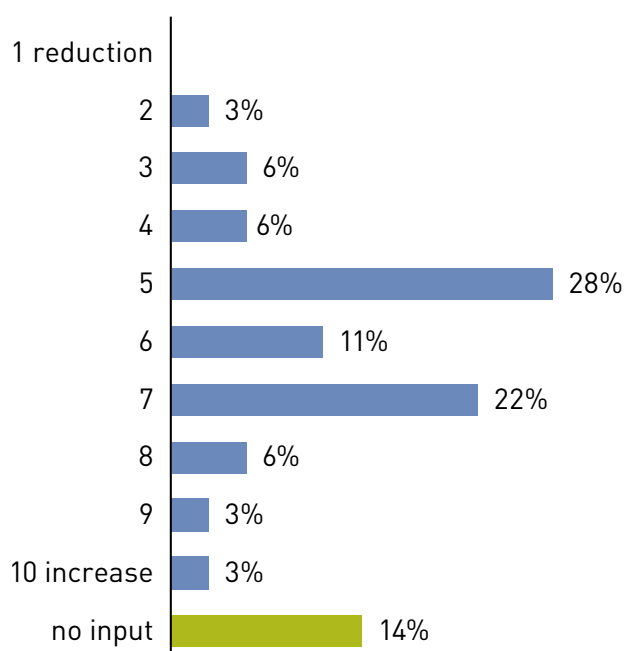
What is your estimate of the impact of BEPS on the competitiveness and the growth potential of your enterprise?



BEPS negative for competitiveness and growth?

- ▶ Three quarters of respondents take an indifferent or negative position regarding the impact of BEPS on the competitiveness and the growth potential of their own enterprise.
- ▶ More than one third of respondents chose the mid range of the evaluation scale. Only 14% regard BEPS as helpful for their own enterprise.
- ▶ Almost 40% of company representatives expect a clear or even very strong reduction of competitiveness for their enterprise as a result of the BEPS Initiative.

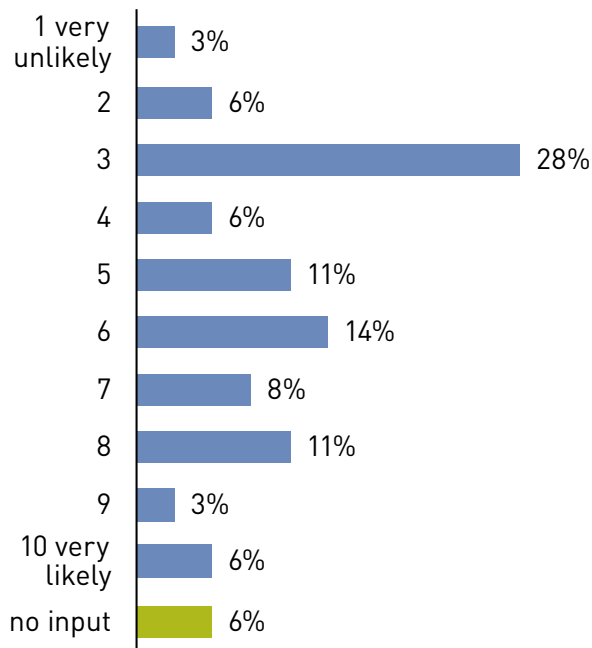
Which impact will the BEPS Initiative most likely have on the group tax rate of your enterprise?



The group tax rate will remain the same

- ▶ The expectations expressed by the respondents do not show a clear picture for a reduction or increase of the group tax rate. Only in individual cases is the expectation for one or the other extreme of the scale.
- ▶ More than 60% of respondents chose the mid points of the evaluation range. They expect that the BEPS Initiative will not have a special impact on the group tax rate.

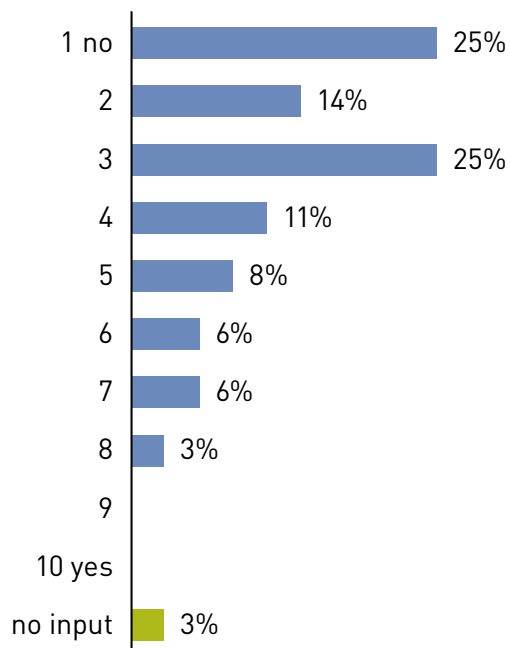
In your view, how likely is it that the BEPS Initiative will remove or clearly reduce the competitive benefits achieved by some enterprises through aggressive tax planning?



BEPS success doubtful for reduction of competitive advantages

- ▶ 37% of the tax experts take the view that they regard the success of the BEPS Initiative to reduce or even eliminate competitive advantages as unlikely or very unlikely.
- ▶ On the other hand 20% take the view that BEPS will likely or very likely be successful.
- ▶ The other respondents have no clear assessment of the chances of success.

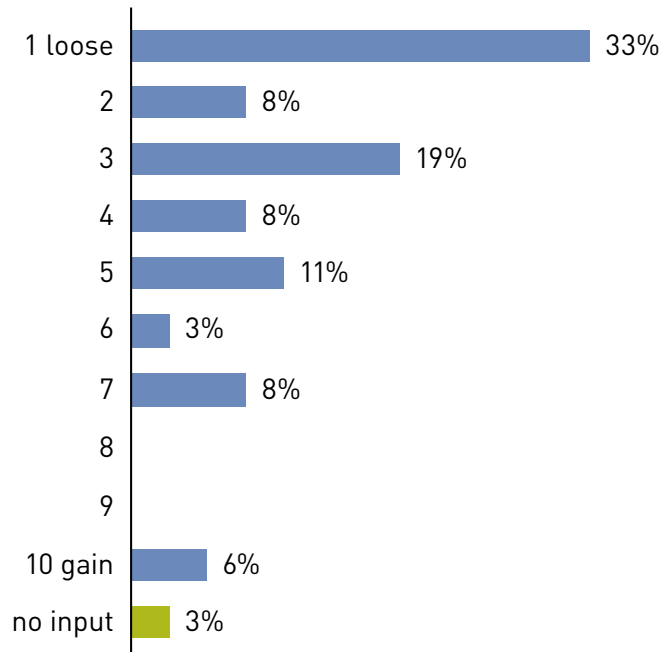
Do the costs triggered by increased compliance requirements observe a reasonable relationship with the advantages of a more just tax competition?



The compliance costs are excessive

- ▶ None of the respondents thinks that the advantages of a more just tax competition have a clearly appropriate relationship with the increased compliance costs.
- ▶ 64% of respondents clearly deny the question and think that compliance costs are unacceptably high for enterprises.

Will German enterprises rather profit or lose as a result of the transformation of Anti-BEPS Measures?



Gains through BEPS only in individual cases, German enterprises will lose

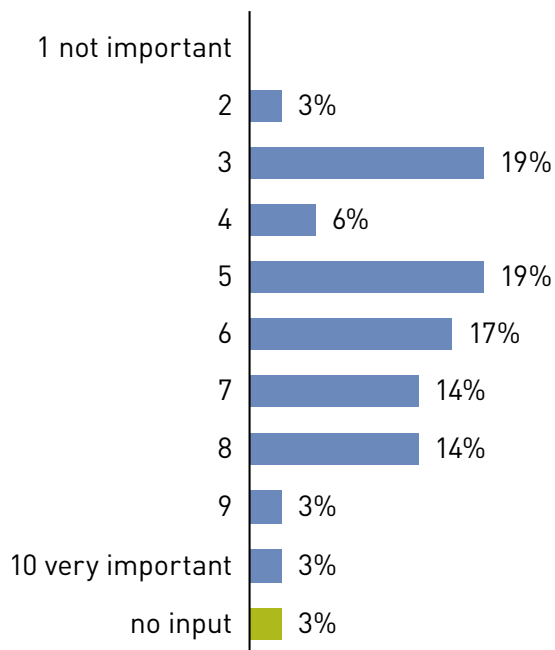
- ▶ The worst evaluation was handed down by 33% of company representatives. They are certain that German companies will, as a result of the Anti-BEPS Measures, lose out. Another 27% more or less agree.
- ▶ Only 6% of respondents take the view that they or rather German enterprises will benefit from BEPS and even win.
- ▶ Altogether about 70% of enterprise representatives associate negative expectations with BEPS. They think that German enterprises will lose out as a result of the conversion of the Anti-BEPS Measures.



F

EU law aspects of BEPS

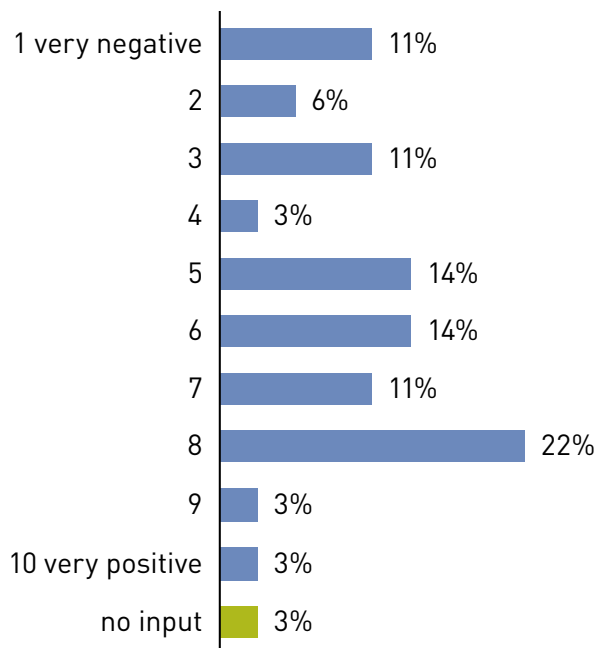
How do you evaluate the introduction of general anti-abuse clauses in the EU Parent-Subsidiary Directive and the EU Interest and Royalty Directive?



EU-anti-abuse clauses are important

- ▶ The introduction of general anti-abuse clauses in the EU Parent-Subsidiary Directive and the EU Interest and Royalty Directive is regarded as important by the majority of respondents.
- ▶ 28% of participants do not allocate specific importance to the provisions to combat abuse in European secondary law.

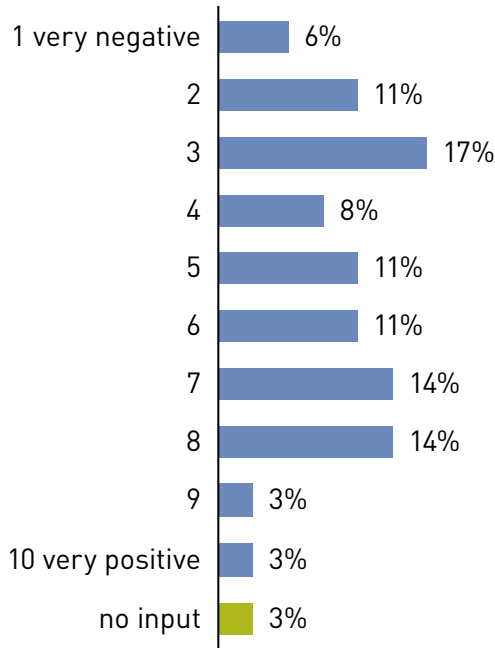
How do you evaluate the introduction of the Common Consolidated Corporate Tax Base (CCCTB) as discussed on the EU level?



CCCTB is welcomed by enterprises

- ▶ The clear majority of participants regard the introduction of CCCTB on the EU level as positive with 28% of respondents even taking a very strong positive view on its introduction.
- ▶ On the other hand, 28% of respondents reject the introduction.

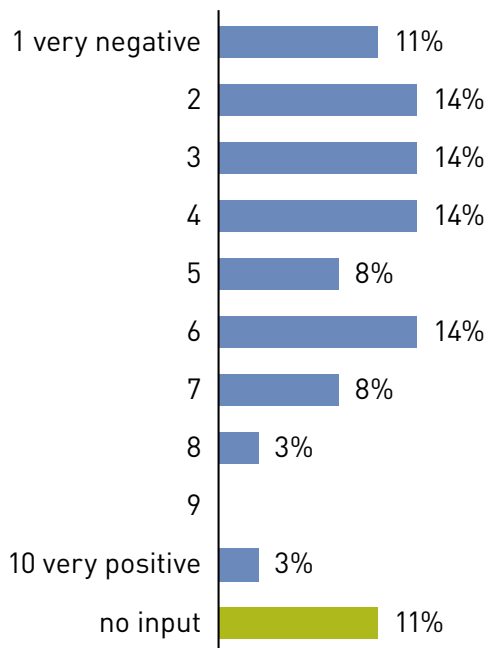
How do you judge the planned introduction on the EU level of an automatic exchange of so-called “Tax Rulings”?



Mixed attitude on Tax Rulings

- ▶ The EU wide introduction of an automatic exchange of Tax Rulings is judged by enterprises as much positively as negatively.
- ▶ A clear tendency for or against the exchange of Tax Rulings cannot be determined in the responses. The substantial number of views falling into the middle range (approx. 44%) shows a high degree of uncertainty.

How do you judge the investigations on the part of the EU Commission in the area of State Aid?



The State Aid investigations are mainly regarded as negative

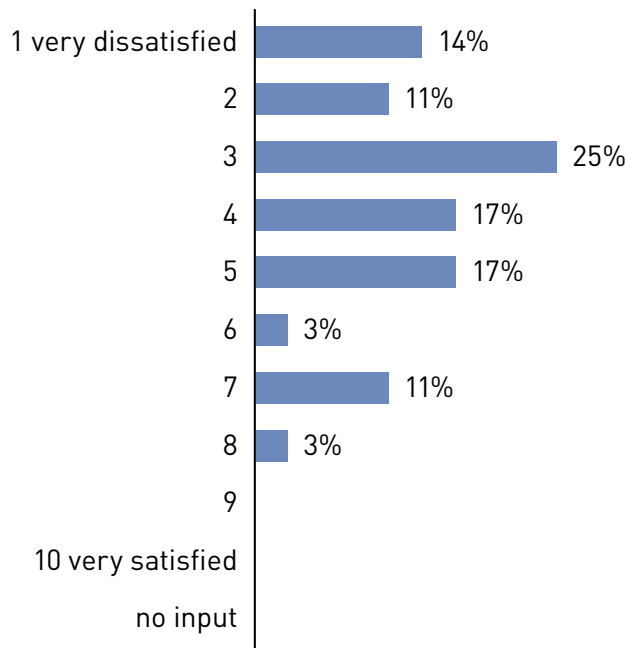
- ▶ Clearly more than half of respondents regard the investigations of the EU Commission in the area of State Aid as negative or very negative.



G

Tax policy aspects of Anti-BEPS Measures

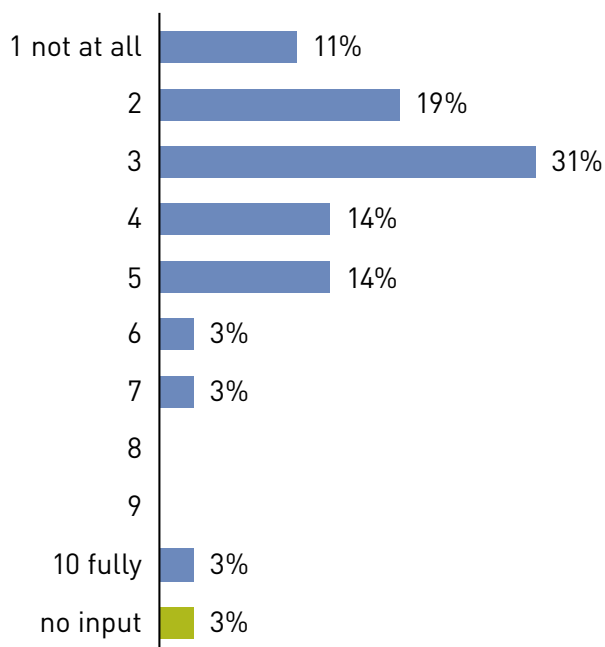
What is your degree of satisfaction concerning how practical enterprise requirements are taken into account at the level of the OECD?



Clear dissatisfaction with the consideration of practical enterprise requirements

- ▶ The clear majority of respondents (approx. 66%) is not satisfied with the consideration of practical enterprise requirements at the level of the OECD, 25% are even very dissatisfied.

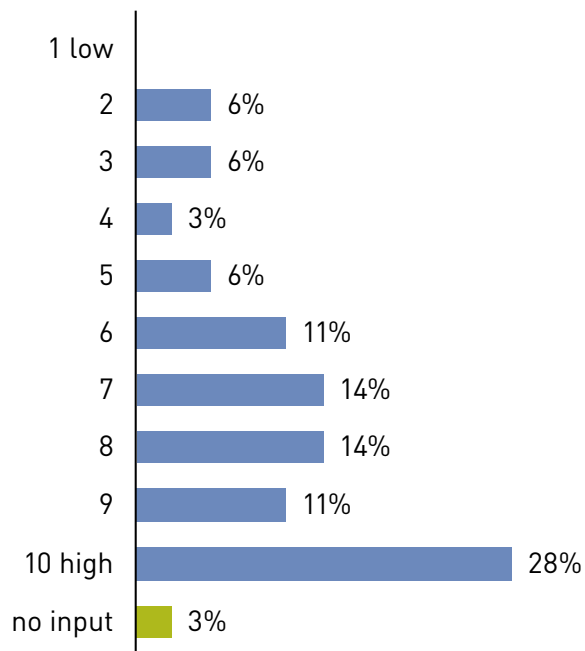
To what extent do tax experts take the view that reasonable interests of internationally active enterprises are taken into account in German tax policy?



Dissatisfaction of tax experts with German tax policy

- ▶ Approx. 75% of respondents do not see the justified interests of internationally active enterprises sufficiently taken into account in German tax policy.
- ▶ There is a clear case for amendments in view of the participants.

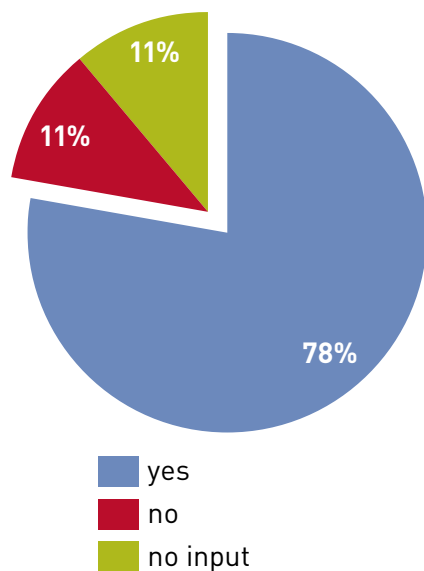
How do you judge the risk resulting from insufficient international consensus when transforming Anti-BEPS Measures and the resulting double taxation?



Lack of international unity in transforming BEPS is a grave danger

- More than three quarters of respondents are seriously concerned that the lack of international consensus in the transformation of Anti-BEPS Measures could lead to double taxation consequences.
- 39% of participants even issued the maximum points of 9 or even 10. They expect that as part of the conversion of Anti-BEPS Measures there will not be international consensus in every case and that the double taxation risk for enterprises will clearly increase in future.

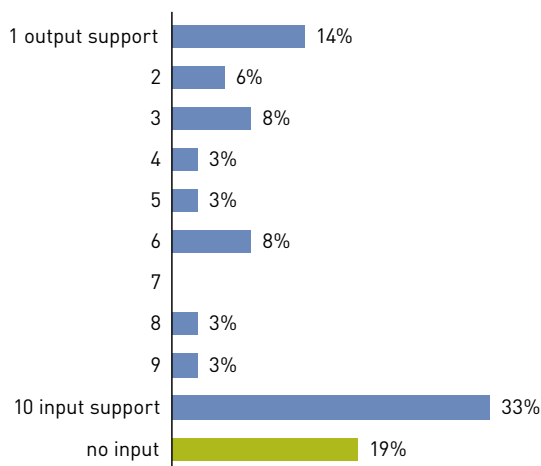
Do you advocate the introduction of tax based research and development incentives in Germany?



Research and development (R&D) should be incentivised in tax

- More than three quarters of respondents clearly recommend the introduction of a tax based research and development incentives .
- In the view of respondents, Germany has a clear need for catching up when compared to other countries.

Would you prefer the tax R&D support as input support (e. g. improved deduction of R&D expenses) or as output support (e. g. reduced tax rate on license income or “Patent-Box”)?



Input support preferred

- › Approximately half the respondents would prefer an input support. 33% of respondents signal a very strong preference for R&D tax incentives (R&D tax credits, support deductions etc.), targeting the cost-side of R&D investment.
- › On the other hand, only 28% of participants prefer the introduction of preferential (effective) tax rates, targeting the exploitation side of R&D investments.

What would be your most important demand regarding German tax policy?

- › Do not create competitive disadvantages for German industry
- › Do not always act as “first mover”
- › Take practical enterprise requirements into account
- › Ratify the Double Tax Treaty with China at long last
- › Protection of German IP
- › Secure tax secrecy/confidentiality
- › Provide for obligatory bilateral consensus for the avoidance of double taxation
- › Immediate increase of capacities for APA- and MAP-handling in the FCTO (Federal Central Tax Office – responsible for administering treaty relief)
- › Introduce arbitration and conciliation mechanisms in treaties

“In view of threatening double taxation and the tax facilitated spying of confidential enterprise data, it is urgently necessary to provide for mandatory and effective mechanisms to settle controversies (‘Baseball Arbitration according to US-model’) in the double tax treaties and to increase the personnel of the negotiating teams. In order to enforce this, CbCR information should only be revealed to such countries, which are prepared to agree on binding standards for settling controversies and the safeguarding of German standards of data protection and tax secrecy.”

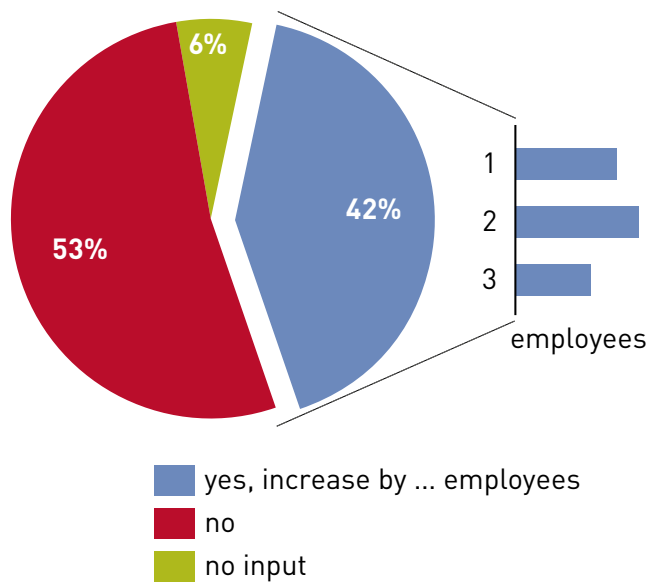
[Note of a participant]



H

Impact of
BEPS Initiative
on tax department

What increase in personnel requirements do you expect for your tax department over the next few years as a result of the BEPS Initiative



42% of enterprises expect the personnel requirements of their tax department to increase as a result of the BEPS Initiative

- On the one hand, the majority of participants do not (as yet) see the need to increase the personnel as result of the BEPS Initiative.
- 42% of respondents note, on the other hand, that the tax department of their enterprise will increase by an average of two employees as a result of the BEPS Initiative.
- A large number of the responding enterprises thus operates on the assumption that the BEPS Initiative will require the availability of additional personnel resources (e. g. as a result of increased compliance requirements).

In which areas will your tax department most likely increase (several mentions possible)?



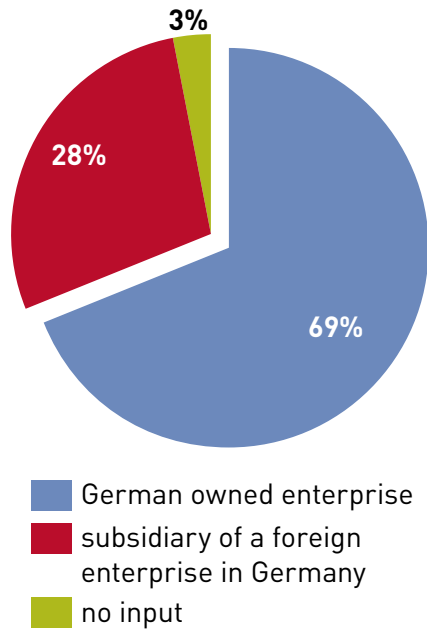
Focus on the areas of transfer pricing and international tax

- In the estimate of the respondents, the BEPS Initiative will cause the greatest and most wide spread personnel requirements for transfer pricing specialists.
- To a lesser extent, additional hirings are to be expected in the area of international tax.
- In the area of domestic tax, there does not appear to be demand for additional personnel in the view of the enterprises.



Information on the respondents

Are you employed with the subsidiary of a foreign enterprise or are you employed in a German owned enterprise?



Design of study

- ▶ The respondents are tax experts from medium sized and large enterprises in Germany. 69% of respondents are employed in a German owned enterprise.
- ▶ The study was conducted with assistance of an online questionnaire.
- ▶ 36 participants gave complete answers in the questionnaire.
- ▶ The interviews took place from November 2015 through February 2016.
- ▶ The evaluation was on an anonymous basis.



Dr. Stephan Schnorberger

Partner

Tel.: +49 211 3 11 16 152

stephan.schnorberger@bakermckenzie.com



Dr. Christian Port

Partner

Tel.: +49 69 29 90 654

christian.port@bakermckenzie.com



Christian Brodersen

Partner

Tel.: +49 69 2 99 08 144

christian.brodersen@bakermckenzie.com

**Baker & McKenzie
Partnerschaft von Rechtsanwälten,
Wirtschaftsprüfern und
Steuerberatern mbB**

Berlin

Friedrichstrasse 88/Unter den Linden

10117 Berlin

Tel.: +49 30 2 20 02 81 0

Dusseldorf

Neuer Zollhof 2

40221 Dusseldorf

Tel.: +49 211 3 11 16 0

Frankfurt am Main

Bethmannstrasse 50-54

60311 Frankfurt am Main

Tel.: +49 69 2 99 08 0

Munich

Theatinerstrasse 23

80333 Munich

Tel.: +49 89 5 52 38 0

www.bakermckenzie.com