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**Committee of Experts on International  
Cooperation in Tax Matters  
Eleventh Session**

Geneva, 19-23 October 2015

Agenda Item 3(a) (iv)

**Base erosion and profit-shifting**

**Subcommittee on Base Erosion and Profit Shifting  
for Developing Countries**

**Report by the Coordinator**

The OECD's Action Plan on Base Erosion and Profit Shifting released in July 2013 (the Action Plan) referred to the interests of developing nations and the role of the United Nations:

“Developing countries also face issues related to BEPS, though the issues may manifest differently given the specificities of their legal and administrative frameworks. The UN participates in the tax work of the OECD and will certainly provide useful insights regarding the particular concerns of developing countries.”

The UN Tax Committee established a Subcommittee on Base Erosion and Profit Shifting Issues for Developing Countries (the Subcommittee) at its ninth session in October 2013.

Initially, the primary function of the Subcommittee was to communicate with officials in developing countries and ensure their views were fed into both the G20/OECD BEPS project as well as the ongoing United Nations tax cooperation work. The mandate of the Subcommittee was expanded in the tenth session of the UN Tax Committee. It now provides as follows:

The Subcommittee is mandated to draw upon its own experience and engage with other relevant bodies, particularly the OECD, with a view to monitoring developments on base erosion and profit shifting issues and communicating on such issues with officials in developing countries (especially the less developed) directly and through regional and inter-regional organisations. This communication will be done with a view to:

- helping inform developing countries on such issues;

- helping facilitate the input of developing country experiences and views into the ongoing UN work, as appropriate; and
- helping facilitate the input of developing country experiences and views into the OECD/G20 Action Plan on Base Erosion and Profit Shifting (BEPS).

The Subcommittee is further mandated to report to the Committee, beginning at the eleventh annual session of the Committee in 2015, on:

- proposed updates to the United Nations Model Convention relating to matters addressed as part of the BEPS Action Plan, with a particular emphasis on the next such update; and
- other possible work relating to base erosion and profit shifting issues that the Committee may wish to undertake or request the Secretariat to undertake.

The Subcommittee released an information note on the project in early 2014. This note, which is available on the UN website, included a questionnaire on how developing countries view and prioritise the BEPS project issues – as well as seeking information on other base erosion concerns. The questionnaire was made available in English, French and Spanish.

Over the years 2014 and 2015 the following countries responded to the questionnaire on BEPS:

Bangladesh	India	Thailand
Brazil	Lesotho	Tonga
Chile	Malaysia	Zambia
China	Mexico	
Ghana	Singapore	

Several other countries also responded but preferred to keep their responses confidential. There were also two submissions by groups of non-governmental organisations: Christian Aid together with Action Aid and the Economic Justice Network together with Oxfam South Africa also provided responses to the questionnaire. The questionnaire and responses, and other relevant documents, are available at <http://www.un.org/esa/ffd/tax-committee/tc-beps.html>

The responses were invaluable in providing a written record of how some developing countries view BEPS and the G20/OECD Action Plan. A short summary of these responses received prior to September 2014 was posted on the abovementioned UN website. A further summary on responses to the questionnaire, following receipt of all the submissions, was published in an article in the special edition of the *Bulletin for International Taxation on Base Erosion and Profit Shifting, Developing Countries' Reactions to the G20/OECD Action Plan on Base Erosion and Profit Shifting* and is also available on the same website.

## **GENERAL CONCLUSIONS**

While there was some variation in both diagnosis and prescription between the respondents and, more importantly, between developing and more developed nations, there is broad consensus on the significance of the issues and the need to work collectively to resolve them.

All respondents said that BEPS affected their tax revenues. Over one-third said that it distorted competition between domestic (generally small) and foreign (generally large) enterprises. Some countries referenced the additional tax burden placed on other taxpayers if multinationals were avoiding tax, and the impacts this could have on voluntary compliance and the development of their economies.

Transfer pricing (including pricing of goods, excessive management fees, royalties, and research and development) was the most commonly raised BEPS issue. Better transfer pricing guidelines and legislation were seen as the primary tools to address it. High interest deductions on related-party debt and concerns about excessive debt levels also featured prominently in their responses. Tax havens, preferential tax regimes and treaty abuse were also cited as causes of BEPS.

A lack of information and capacity building were also common themes. Revenue authorities in developing nations struggle to establish, grow and up-skill effective international tax teams. Some respondents cited poorly developed EOI networks as being an impediment while others had networks in place but found that information was not exchanged quickly enough.

All of the respondents agreed that the Action Plan items identified by the Subcommittee in the questionnaire as developing nation priorities were important, with disclosure of aggressive tax positions (Action 12) and transfer pricing documentation (Action 13) being the top concerns. This was closely followed by the transfer pricing actions on intangibles (Action 8) and other high-risk transactions (Action 10), which includes management fees.

There was less agreement over whether other Actions not prioritised in the questionnaire are nevertheless important to developing countries. However, the avoidance of permanent establishment status (Action 7) and the digital economy (Action 1) are the two Actions that were most commonly cited in response to this question.

## **THE FINAL BEPS PACKAGE**

The first seven Reports on BEPS issues were presented to the G20 Leaders at the Brisbane Summit in 2014.

The final BEPS package, including and consolidating the first seven 2014 Reports, was released on 5 October 2015. It was transmitted to the G20 for endorsement by Finance Ministers at their meeting on 8 October and will be further endorsed by G20 Leaders at the Antalya Summit on 15-16 November 2015.

The Final Reports for each Action, which together with the Explanatory Statement comprise the BEPS package, are as follows:

- Action 1 – Addressing the Tax Challenges of the Digital Economy
- Action 2 – Neutralising the Effects of Hybrid Mismatch Arrangements
- Action 3 – Designing Effective Controlled Foreign Company Rules
- Action 4 – Limiting Base Erosion Involving Interest Deductions and Other Financial Payments
- Action 5 – Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance
- Action 6 – Preventing the Granting of Treaty Benefits in Inappropriate Circumstances
- Action 7 – Preventing the Artificial Avoidance of Permanent Establishment Status
- Action 8-10 – Aligning Transfer Pricing Outcomes with Value Creation
- Action 11 – Measuring and Monitoring BEPS
- Action 12 – Mandatory Disclosure Rules
- Action 13 – Transfer Pricing Documentation and Country-by-Country Reporting
- Action 14 – Making Dispute Resolution Mechanisms More Effective
- Action 15 – Developing a Multilateral Instrument to Modify Bilateral Tax Treaties

The Explanatory Statement provides a high level description of the process involved in producing the package of measures. It notes that the package is the result of both OECD and G20 countries working together on an equal footing<sup>1</sup>.

## **UPDATES TO THE UNITED NATIONS MODEL DOUBLE TAXATION CONVENTION**

As mentioned above the mandate of the Subcommittee was expanded at the tenth session.

The Subcommittee is further mandated to report to the Committee, beginning at the eleventh annual session of the Committee in 2015, on:

- proposed updates to the United Nations Model Convention relating to matters addressed as part of the BEPS Action Plan, with a particular emphasis on the next such update; and
- other possible work relating to base erosion and profit shifting issues that the Committee may wish to undertake or request the Secretariat to undertake.

The Reports on Actions 2, 6, 7 and 15 contain measures that will change the OECD Model Tax Convention, and may be incorporated into a Multilateral Instrument.

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<sup>1</sup> Non OECD members actively participating in the work included Albania, Argentina, Bangladesh, Brazil, Colombia, Costa Rica, People's Republic of China, Croatia, Georgia, Indonesia, Israel, Jamaica, Kenya, Lithuania, Morocco, Nigeria, Peru, Philippines, Russian Federation, Saudi Arabia, Senegal, Tunisia, and Vietnam.

## **The Report on Action 2 – Neutralising the Effects of Hybrid Mismatch Arrangements**

The Report on Action 2 contains a proposal for a new treaty provision to address treaty problems associated with hybrid entities. This issue is currently an item on the agenda for the Committee (*refer to item 3(a)(i) Article 1 (Persons covered): application of treaty rules to hybrid entities*). Accordingly, no further work needs to be undertaken in this Subcommittee at this stage.

## **The Report on Action 6 – Preventing the Granting of Treaty Benefits in Inappropriate Circumstances**

The Report on Action 6 falls into three areas:

- A. *Develop model treaty provisions and recommendations regarding the design of domestic rules to prevent the granting of treaty benefits in inappropriate circumstances;*
- B. *Clarify that tax treaties are not intended to be used to generate double non-taxation; and*
- C. *Identify the tax policy considerations that, in general, countries should consider before deciding to enter into a tax treaty with another country.*

The Report proposes the following categories of changes to the OECD Model Tax Convention (including related Commentaries) including:

- ***1. Changes to the title and preamble*** to clarify that the Contracting States, when entering into a treaty, wish to prevent tax avoidance and, in particular intend to avoid creating opportunities for treaty shopping.
- ***2. Inclusion of anti-abuse rules in treaties to address treaty shopping and other specific forms of treaty abuse.***
- ***3. Inclusion of targeted new rules in tax treaties to address specific treaty abuse issues relating to dual resident entities, dividends, shares in land rich companies, and third state PEs.***
- ***4. New Commentary on Tax Policy Considerations that are relevant for countries to consider before deciding*** to enter into a tax treaty with another country.

As a general proposition, the underlying direction of these proposals are aimed at clarifying that treaty abuse is not acceptable and that treaty benefits should not be available in situations where they were not intended to be granted. It also highlights the position that treaties are not intended to facilitate double non-taxation.

## **The Report on Action 7 – Preventing the Artificial Avoidance of a Permanent Establishment**

The 2013 Action Plan called for changes to the definition of a PE to prevent the artificial avoidance of PE status in relation to BEPS, including through the use of commissionaire arrangements and the specific activity exemption. It was also suggested that work on these issues should address related profit attribution issues. To that end, the Report proposes specific treaty changes to the definition of PE in Article 5 to address:

- A. Artificial avoidance of PE status through commissionaire arrangements and similar strategies;*
- B. Artificial avoidance of PE status through the specific activity exemptions;*

The Report also proposes alternative provisions in the Commentary to the OECD Model to address

- C. Other strategies for the artificial avoidance of PE status (eg contract splitting).*

## **The Report on Action 15 – Developing a Multilateral Instrument to Modify Bilateral Tax Treaties**

The Report on Action 15 assesses the feasibility of a multilateral instrument to implement the BEPS treaty-related changes and amend bilateral tax treaties. The conclusion is that a multilateral instrument is feasible for the efficient implementation of new treaty provisions.

In terms of process, an ad-hoc group, open to participation by all countries has been established to develop the multilateral instrument. The aim is to have the instrument ready for signature in 2016.

## **THE FUTURE WORK OF THE SUBCOMMITTEE FOR 2016**

The Subcommittee should report to the Committee on whether proposals in the Reports on Action 6 and Action 7 should be adopted for the United Nation Model Tax Convention. It may be necessary to consider whether some proposals should be prioritised over other in determining changes for the next update. This report may also consider alternatives to the proposals in those Reports

The Subcommittee should also report to the Committee on any information regarding the development of the multilateral instrument.

The Subcommittee may also consider whether there are other changes to the treaty that should be considered to address BEPS issues.

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