

Developing Countries' Reactions to the G20/OECD Action Plan on Base Erosion and Profit Shifting

This article describes and examines the reactions of developing countries to the G20/OECD Action Plan on Base Erosion and Profit Shifting as communicated to the Subcommittee on Base Erosion and Profit Shifting Issues for Developing Countries of the UN Committee of Experts on International Cooperation in Tax Matters.

1. Introduction

The decision by the G20 and the OECD to jointly consider ways of countering base erosion and profit shifting reflected a realization that these issues adversely affect all jurisdictions. Clearly, this issue is not just relevant to developed economies.¹

Although base erosion and profit shifting has the potential to affect all nations, it is by no means axiomatic that its effect is uniform or that countries at different stages of development would agree on how best to address the issue. Recognizing this, the UN Committee of Experts on International Cooperation in Tax Matters (UN Tax Committee) asked developing countries to provide their views on this subject, in particular, their perspectives on fair and appropriate means of responding to the challenges imposed by base erosion and profit shifting.

Since the beginning of 2014, the following 13 developing countries have publicly responded to a UN Tax Committee questionnaire (the questionnaire)² on base erosion and profit shifting:

- Bangladesh;
- Brazil;
- Chile;
- China (People's Rep.);

- Ghana;
- India;
- Lesotho;
- Malaysia;
- Mexico;
- Singapore;
- Thailand;
- Tonga; and
- Zambia.

Several other countries also responded but preferred to keep their responses confidential. Two non-governmental organizations, i.e. Christian Aid & ActionAid and the Economic Justice Network, as well as Oxfam South Africa, also provided responses to the questionnaire.

2. Background to the Questionnaire

The OECD's Action Plan on Base Erosion and Profit Shifting (BEPS) (the Action Plan), which was released in July 2013, refers to the interests of developing nations and the role of the United Nations, in the following words:

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.^{3,4}

Subsequently, 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 are appreciated by both the G20/OECD BEPS initiative and the ongoing work of the United Nations on tax cooperation. The mandate of the Subcommittee was expanded in the tenth session of the UN Tax Committee as follows:

The Subcommittee is mandated to draw upon its own experience and engage with other relevant bodies, particularly the OECD,

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1. In June 2012, the G20 leaders discussed the need to counter base erosion and profit shifting at their meeting in Mexico. They asked the OECD to report to them on the issue. The OECD released a report in 2013 outlining the problems and promised an Action Plan by mid-2013. The latter was published as OECD, *Action Plan on Base Erosion and Profit Shifting* (OECD 2013), International Organizations' Documentation IBFD, also available at www.oecd.org/ctp/BEPSActionPlan.pdf.
2. The questionnaire and responses, and other relevant documents, are available at www.un.org/esa/ffd/tax-committee/tc-beps.html.

3. OECD, *supra* n. 1, at p. 26.
4. The effect of base erosion and profit shifting on developing countries is a strong focus for international organizations. In this regard, it should be noted that the OECD, *Part 1 of a Report to G20 Development Working Group on the Impact of BEPS in Low Income Countries* (OECD July 2014), available at www.oecd.org/tax/part-1-of-report-to-g20-dwg-on-the-impact-of-beps-in-low-income-countries.pdf and *Part 2 of a Report to G20 Development Working Group on the Impact of BEPS in Low Income Countries* (OECD Aug. 2014), available at www.oecd.org/ctp/tax-global/part-2-of-report-to-g20-dwg-on-the-impact-of-beps-in-low-income-countries.pdf.

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 organizations. This communication will be done with a view to:

- helping inform developing countries on such issues;
- 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.⁵

In this context, the Subcommittee released an information note on the project in early 2014. This note, which is also available on the UN website,⁶ included a questionnaire on how developing countries view and prioritize issues regarding the BEPS initiative, as well as seeking information on other base erosion concerns. The questionnaire was made available in English, French and Spanish.

The responses to the questionnaire have been invaluable in providing a written record of how some developing countries view the BEPS initiative and the G20/OECD Action Plan. A short summary of these responses was posted on the UN website in September last year.⁷

This article provides further detail on the responses of participating countries to the questionnaire. In this regard, some graphs illustrating the relative weighting of various responses have been included.⁸

The overall finding is that, while there is 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 regarding the BEPS initiative. There is, therefore, a need to work collectively to resolve these issues.⁹

The G20 and OECD continue to focus on the participation of developing countries in the BEPS initiative. In its “Strategy”, published in November 2014, which was wel-

comed by G20 Leaders at their Summit later that month, the OECD proposed a new structured dialogue process, based on the following three interconnected pillars:

- (1) direct participation of developing countries and regional tax organizations in the OECD Committee on Fiscal Affairs (CFA) and its subsidiary bodies;
- (2) regional networks of tax policy and tax administration officials on the BEPS initiative in five specific regions; and
- (3) capacity building support through mentoring, and the development of toolkits in collaboration with international regional organizations and developing countries working in the context of the regional networks.¹⁰

3. Developing Countries’ Reactions to the BEPS Initiative

3.1. Introductory remarks

Question 1 (*see* section 3.2.) and questions 2, 3 and 4 (*see* sections 3.3., 3.4. and 3.5., respectively) were asked to gain insight into how developing countries perceive both the causes and effects of base erosion and profit shifting in their jurisdictions.

3.2. Question 1

How does base erosion and profit shifting affect your country?

All respondents confirmed that base erosion and profit shifting affected their countries, with most citing the effect on tax revenue as a chief concern. A few respondents noted that they had no formal quantitative measure of the extent of the lost tax revenue; however, they seemed very aware that low effective tax rates applied to income sourced in their countries.

It was noted that one obvious consequence for countries is that the focus of revenue collection moves to consumer taxes that are easier to collect, such as VAT. Similarly, tax authorities direct their operational resources at those taxpayers who cannot move their income, for example, local individual residents together with those entities that do not have the opportunity or, indeed, the resources to engage in tax planning, such as small and medium-sized enterprises (SMEs).

Countries observed that these consequences of base erosion and profit shifting have adverse implications for perceptions of fairness and integrity in their tax systems. This, in turn, undermines voluntary compliance, which is crucial to the effective administration of all income tax systems, including those of developing countries.

It was noted by some that base erosion and profit shifting concerns are particularly pressing for developing countries. This is because of the capital import nature (CIN) of those countries, their reliance on corporate income tax and the extent of foreign ownership of their businesses.

5. The mandates of all the Subcommittees of the UN Tax Committee are available at www.un.org/esa/ffd/tax-committee/tc-current-subcommittees.html.

6. This can be found at www.un.org/esa/ffd/tax/BEPS_request.pdf and www.un.org/esa/ffd/tax/BEPS_note.pdf.

7. *See* www.un.org/esa/ffd/wp-content/uploads/2015/01/10STM_CRP12_BEPS.pdf.

8. It should be noted that individual country positions are not identified. As a result, this article is not a substitute for reading the views given by participants.

9. The general themes emerging from the responses to the questionnaire are in line with the IMF, *Spillovers in International Corporate Taxation Policy Paper* (IMF 2014), available at www.imf.org/external/np/pp/eng/2014.pdf. Also of note is a recent UN Working Paper on *Foreign Direct Investment, Tax and Development*, version 2.1 as at 11 May 2015 (UN 2015), available at <http://investmentpolicyhub.unctad.org/Blog/Index/42>.

10. OECD, *Strategy for Deepening Developing Country Engagement in the BEPS Project* (OECD 2014), available at www.oecd.org/ctp/strategy-deepening-developing-country-engagement.pdf.

There was a view that the effects of base erosion and profit shifting on the administration of taxes means that, in practice, their tax systems are regressive, even though there is no intention to be regressive in terms of underlying policy objectives or income tax law. Some respondents noted that this unintended gap between tax policy objectives and results may be hindering the development of their economies. Linked to this is a concern that development of physical and legal infrastructures to encourage foreign investment was not rewarded by the revenue collection from such investment.

Concerns were also expressed that the lack of sophistication in tax laws makes developing countries particularly vulnerable. This lack of sophistication typically evidenced itself in the absence of controlled foreign company (CFC) rules, no general anti-avoidance rules (GAARs) and an over-reliance on formalistic legal systems.

3.3. Question 2

If you are affected by base erosion and profit shifting, what are the most common practices or structures used in your country or region, and the responses to them?

Transfer pricing is viewed as the most significant contributor to base erosion and profit shifting. Respondents identified various forms of transfer pricing that were of concern. There was a common concern regarding the pricing of goods going both in and out of developing countries. Equally, there was a strong perception that management fees and head-office services were overvalued. Tax deductions for payments in respect of these services were perceived as a common technique for shifting profits. Similarly, a number of respondents raised the pricing of royalty payments for intellectual property as a base erosion and profit shifting problem. Some respondents referred to the imposition of limits on deductions for royalties and the imposition of withholding tax on services as a way of responding to these concerns.

There was a common perception among respondents that revenue was not being collected when the economic activity took place because of a perceived disconnect between the economic activity and when the income is reported for tax purposes. This is often achieved by shifting risk contractually through a business restructuring to plan for when profits are reported. At the same time, some reported that they believe that the value of local activity, such as local marketing activities, was not recognized and adequately compensated.

Over half of the respondents referred to transfer pricing legislation as a response to base erosion and profit shifting. Some reported that they have recently enacted transfer pricing legislation. Others have strengthened existing transfer pricing legislation or have introduced controls and documentation requirements.

Not unexpectedly, some countries observed that enacting rules is one thing, but having the capacity to apply the rules is something else. Several respondents indicated that countries have increased transfer pricing resources by creating special transfer pricing units and increasing capac-

ity in terms of staff in international taxation and technical training. One respondent noted that efforts to increase the focus on transfer pricing audits had been effective in ensuring that higher profits were reported or declared in that country. At a more practical level, one country stated that it has conducted a transfer pricing consultation programme to remind taxpayers to keep good documentation. It also saw merit in concluding bilateral advance pricing agreements (APAs) that leverage off the OECD's guidelines on arm's length pricing.

Another common complaint related to what was considered to be non-commercial levels of debt funding of foreign-owned entities. Respondents said that debt levels were often artificially high and indefensible. Several also referred to the use of high interest rates on related-party debt. The obvious result in both cases is the shifting of profit out of the jurisdiction by way of interest deductions. A few respondents identified the use of thin capitalization rules as a way of countering these practices.

Tax havens and preferential regimes were raised by many respondents as a major part of the base erosion and profit shifting problem. They observe considerable shifting of profits to low- or no-tax jurisdictions that do not exchange information regarding capital stock structure, ownership of assets or transactions. Some countries complained about the migration of intellectual property to low-tax jurisdictions. A few countries addressed this by imposing limits or additional requirements in relation to deductible payments made to tax havens.

In the context of tax treaties, some countries were focused on the ability of multinational enterprises (MNEs) to avoid establishing a permanent establishment (PE), especially if the business model did not require a physical presence. Others specifically referred to treaty abuse, particularly in connection with the use of tax havens. One respondent proposed reconsideration of treaty positions and/or to commence renegotiations of tax treaties, particularly those tax treaties that are commonly used for treaty shopping. One country cited continued emphasis for source-based taxation in tax treaties as a response to base erosion and profit shifting. Overall, developing countries recognize that typical profit shifting techniques are most effective when used in combination with: (1) payments to tax havens; (2) harmful preferential regimes; and/or (3) treaty abuse.

Two respondents stated that their ability to counter base erosion and profit shifting was hindered by the fact that they did not have tax treaties or tax information exchange agreements. Another approach that was suggested was to impose higher withholding rates on payments to low-tax jurisdictions.

Other concerns raised, in each case by a couple of respondents, included:

- The emergence of the digital economy as a general matter: one respondent specifically identified the sale of tourism packages over the Internet for tourism services provided in their country. Another was concerned with regard to the sale of goods and services

over the Internet to residents more generally. One country stated that it had amended VAT legislation to require foreign providers of electronic services to register for VAT.

- Tax incentives: a few respondents noted that their policy to provide tax incentives to new investment in selected sectors was causing base erosion and profit shifting problems. As a response, at least one country has scaled down tax holidays and rationalized treaty incentives.
- Manipulation of tax residence: one country stated that the artificial transfer of tax residence was a concern.
- High-net-worth individuals: a couple of respondents cited high-net-worth individuals as giving rise to base erosion and profit shifting issues.

As a general comment, a number of countries noted that they have also relied on their source rules, GAARs or other domestic anti-abuse legislation to counter perceived abuses.

3.4. Question 3

When you consider an MNE's activity in your country, how do you judge whether the MNE has reported an appropriate amount of profit in your jurisdiction?

In terms of administrative processes, most countries observed, as a starting point, that they adopted the same law and practices that they used for all taxpayers in their jurisdiction. In other words, they routinely start with normal assessment practices used for all taxpayers by reviewing annual return filing and any other relevant contemporaneous documentation. Many respondents confirmed that they would undertake some form of risk profiling in advance of a decision to audit foreign-owned firms. For some countries, this was a recent development designed to use scarce audit resources more effectively.

Risk assessment techniques took various forms. Some countries noted the importance of undertaking an economic analysis of the particular industry in which the MNE operates. In that context, the cooperation of industry bodies in providing information regarding wider industry trends and predictions is highly valued in performing this exercise. These countries also noted that they would study whether the industry's profitability was increasing or decreasing and then compare those results with the results of the MNE concerned.

Many respondents also noted the importance of comparing the performance of an MNE with other taxpayers in the industry. This was particularly undertaken within the context of the comparable results of local firms of similar size and structure when this information is available. Decisions to audit are also influenced by measuring the effective tax rate by comparing accounting profits with the amount of tax paid.

Another approach is to examine the extent of related-party transactions, paying particular attention if a decline in taxable profits is matched by an increase in related-

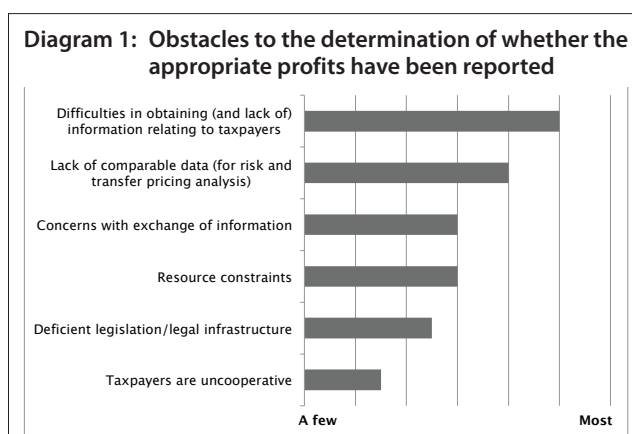
party transactions. Countries also counted the existence of transactions with tax havens as a relevant risk-profiling factor. A number of countries said that they would focus on any significant payments to non-residents.

Some countries stated that taxation should be aligned with substance, so that the allocation of profits should follow substantive economic activities that are undertaken, and that the best way to achieve this is to have robust transfer pricing guidelines supporting the arm's length principle. A number of countries also use a strict matching rule for deductions where deductions have to be closely matched to the income that is being produced. Other countries noted the importance of checking that, at least, withholding obligations had been met on payments of passive income, i.e. dividends, interest, royalties and rent.

3.5. Question 4

What main obstacles have you encountered in assessing whether the appropriate amount of profit is reported in your jurisdiction and in ensuring that tax is paid on such profit?

In one way or another, a recurring theme emerged centred on lack of information and transparency. This is illustrated in Diagram 1.



As a starting point, countries were generally concerned regarding the lack of information in relation to the actual taxpayer. These countries identified lack of information and transparency with regard to the global value chain as a key obstacle to determining whether reported earnings are consistent with the functions and risks of the local entity or branch.

There was general concern regarding the lack of relevant information in connection with foreign related parties or, indeed, the entire global group, especially in a world where the volume and complexity of intra-group trade is so significant. Some countries noted the importance of Action 13, i.e. country-by-country reporting in the BEPS initiative, in this context. Other respondents indicated that MNEs do not cooperate in supplying the relevant information or fail to supply such information in a timely manner.

Another common complaint was the lack of comparable data on which to base a transfer pricing case. Countries noted a lack of comparable companies in terms of size or in terms of the relevant industry or sector. The respondents

also referred to the lack of available public information on comparable local entities or the relevant industry group.

Other perceived causes of lack of information included the absence of fully functioning exchange of information (EOI) arrangements. In some cases, this was in the absence of a treaty network generally. The lack of effective EOI was a concern, particularly in relation to low-tax jurisdictions. At a practical level, concerns reiterated the lengthy time it took for information to be provided, even when EOI arrangements are in place.

Apart from a lack of information, the other main barrier for countries is the lack of expertise and resources to analyse available data and then apply relevant measurement and risk assessment tools. This comes down to both a lack of technical skills and insufficient resources. Countries specifically referred to the value they placed on the practical assistance received from the International Monetary Fund (IMF), the World Bank and the OECD in this regard.

Finally, a few respondents stated that a major obstacle was inadequate legislation and a deficient legal infrastructure.

4. Developing Countries' Reactions to the Action Plan

4.1. Introductory remarks

Six questions were posed regarding the reactions of developing countries to the Action Plan, i.e. questions 5, 6, 7, 8, 9 and 10 (see sections 4.2., 4.3., 4.4., 4.5., 4.6. and 4.7., respectively).

4.2. Question 5

Do you agree that these [eight action points identified below] are particularly important priorities for developing countries?

The Action Plan contains 15 separate action items. The Subcommittee hypothesized that 8 of the 15 action items would be of the most importance to developing countries, on the basis that those actions would either (i) provide more support to source state taxation, albeit within current frameworks, or (ii) improve transparency between MNEs and tax authorities. These eight action items are:

- (1) Action 4 – Limit base erosion via interest deductions and other financial payments;
- (2) Action 6 – Prevent the granting of treaty benefits in inappropriate circumstances;
- (3) Action 8 – Assure that transfer pricing outcomes are in line with value creation: intangibles;
- (4) Action 9 – Assure that transfer pricing outcomes are in line with value creation: risks and capital;
- (5) Action 10 – Assure that transfer pricing outcomes are in line with value creation with reference to other high-risk transactions, in particular, management fees;
- (6) Action 11 – Establish methodologies to collect and analyse data on base erosion and profit shifting, and the actions to address it;
- (7) Action 12 – Require taxpayers to disclose their aggressive tax planning arrangements; and

- (8) Action 13 – Re-examine transfer pricing documentation.

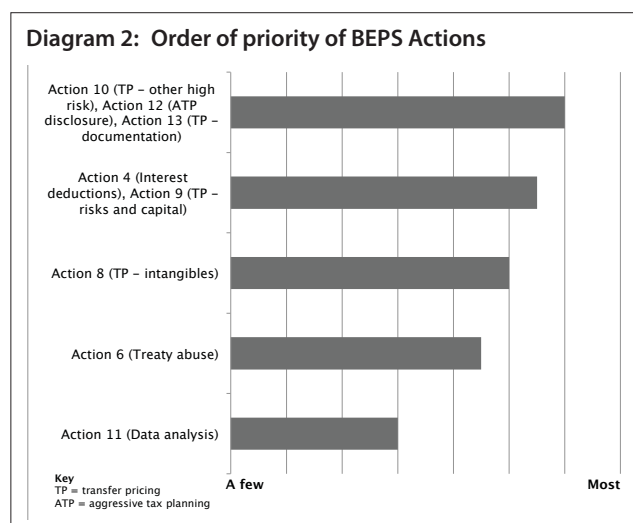
Countries were asked if they agreed that the eight selected action items were, in fact, the most important action items for them.

While most respondents agreed with the priorities as listed above, a good number also indicated that the other action items were still very important to them. One responded that it was not possible to generalize for developing countries as the circumstances of these countries were so diverse.

4.3. Question 6

Which of these OECD's action points do you see as being most important for your country, and do you see that priority changing over time?

Following from question 5 (see section 4.2.), countries were asked to indicate their order of priority in relation to those particular action points. The responses are illustrated in Diagram 2.



An overwhelming number of respondents identified the transfer pricing Actions 8, 9, 10 and 13 as being of utmost importance to them. Even so, there was a slight weighting in favour of the work being pursued in Action 10 (high-risk transactions, management fees) and Action 13 (transfer pricing documentation) compared with Action 8 (intangibles) and Action 9 (allocation of risk and capital).

Two other action points ranked as being nearly as important as transfer pricing. The issues being addressed by Action 4 (interest deductions and other financial payments) attracted a significant amount of interest for developing countries. Countries also prioritized Action 12 (aggressive tax planning arrangements) as being of real concern in countering base erosion and profit shifting in their countries. The identification of these top priorities reveals a high level of consistency in terms of the responses to question 2, which identified transfer pricing and interest deductibility as key causes of base erosion and profit shifting.

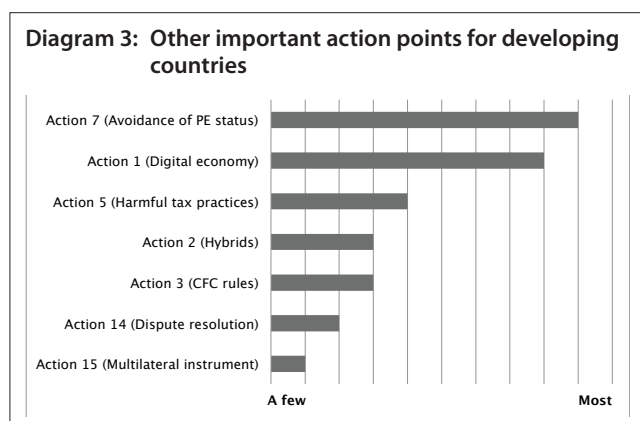
Following close behind these top action items, countries rated Action 6 (treaty abuse) as a key priority. Underpinning this was a clear concern that current treaty arrangements were prejudicial to them because of treaty abuse and a sense that they had agreed to tax treaties that were producing base erosion and profit shifting due to links to harmful preferential regimes and treaty shopping.

Countries also expressed enthusiasm for the work in Action 11 (data collection and analysis) as they view the long-term future of resolving base erosion and profit shifting as being connected to significantly better sources of information. (Again, this is consistent with the responses given by countries to question 4 (see section 3.5.) on the obstacles that countries encountered in ensuring that appropriate levels of profit are declared or reported in their countries.)

In addition, countries were asked if they saw priorities changing over time. A few indicated that progress on some action items, e.g. Actions 12 and 13, might result in a greater focus on the issues addressed by Actions 8 and 9. Others thought that changes to priorities might be driven by better information and analysis as a result of the work on Action 11. A number of countries thought that their assessment of their current top priorities would be unlikely to change for some time to come.

4.4. Question 7

Are there other action points currently in the Action Plan but not listed above that you would include as being most important for developing countries?



Around half of the respondents identified the work undertaken in relation to Action 7 (avoidance of PE status) as highly relevant to them. This reflects their concern that MNEs have used strategies to avoid having a taxable presence in their country. (In this respect, see section 3.3. for the responses to question 2.) This is also linked to the concern that such countries had agreed to treaty provisions that might have contributed to base erosion and profit shifting.

Almost half of respondents signalled a strong interest in Action 1 (the digital economy). Indeed, along with Action 11, Action 1 appeared to be regarded as the action item most likely to produce the most long-term systematic

response to base erosion and profit shifting in developing countries.

Countries also identified Action 5 (countering harmful tax practices) as important. This response is consistent with the responses received in relation to question 2 (see section 3.3.) that identified the role of tax havens and preferential regimes as key causes of base erosion and profit shifting.

4.5. Question 8

Having considered the issues outlined in the Action Plan and the proposed approaches to addressing them (including domestic legislation, bilateral treaties and a possible multilateral treaty), do you believe there are other approaches to addressing those practices that might be more effective at the policy or practical levels instead of, or alongside, such actions for your country?

Some countries answered “no” to question 8 and to question 9 (see section 4.6.). These responses appear to reflect a view that the Action 6 approaches were sufficiently comprehensive as an initial way forward to countering base erosion and profit shifting, including for developing countries. Realistically, it also reflects the resource constraints countries face in reacting to any reform project, including those that are being driven internationally. Other countries, however, had a variety of different suggestions in response to the question of whether other approaches, which were not included in the Action Plan, should be explored.

Many countries took the opportunity to reinforce the point that capacity building was crucial to implement the deliverables arising from the Action Plan. Some suggested developed countries should provide developing countries with their experience on counteracting base erosion and profit shifting by way of technical assistance. Other respondents emphasized the need for international organizations, such as the United Nations, the IMF, the OECD and the World Bank, to provide particular support to achieve the objectives in the Action Plan.

Some answers emphasized specific practical initiatives, such as work to improve risk analysis tools, training, particularly in relation to transfer pricing, and the use of supervision techniques alongside audits to improve taxpayer compliance. One respondent advocated a special project to deal more directly with business restructuring. Another suggestion was that developing countries should be given more assistance from international organizations as to how tax authorities in developing countries should organize staff and budgets in relation to international tax work. The idea was that countries needed very specific standards and guidance on the numbers of people and the types of skills that are realistically needed for this kind of work.

Another suggestion was that new rules produced by the Action Plan be entrenched in the domestic law of countries without the overuse of multilateral instruments and guidance. This seemed to reflect a concern that international guidelines did not carry sufficient weight in jurisdictions to ensure either their application or compliance with them.

Several countries commented that generally achieving effective implementation of the BEPS initiative depended on obtaining the “buy-in” of developing countries. It was proposed that the United Nations, the OECD and the World Bank should provide more technical guidance on gaps in domestic law, tax treaties and transfer pricing guidelines. Another suggestion was that the United Nations should produce its own guidance on the 15 points of the Action Plan. (This has been adopted as part of the mandate of the Subcommittee.) Another idea was to establish a multilateral forum along the same lines as the Global Forum on Transparency and Exchange of Information. Other ideas included expanding the tax sections of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations,¹¹ and requiring MNEs to include commitments not to pursue base erosion and profit shifting strategies in their corporate governance documents.

4.6. Question 9

Having considered the issues outlined in the Action Plan, are there are other base erosion and profit shifting issues in the broad sense that you believe may deserve consideration by international organizations such as the United Nations and the OECD?

Some countries replied “no” or “not for now”. Other respondents suggested exploring the following streams of work:

- encouraging developing countries to adopt a GAAR as well as specific anti-avoidance rules in their domestic law;
- pursuing work on the taxation of capital gains under domestic law and under tax treaties;
- rebalancing source versus residence taxation, especially in relation to tax treaties;
- the treatment of branch profits;
- the cash economy; and
- the adverse consequences of the use of tax incentives.

A number of countries responded that improving transparency and EOI networks is critical. One respondent suggested that the use of regional multilateral agreements on EOI and assistance in collection should be promoted.

4.7. Question 10

Do you want to be kept informed by email on the Subcommittee’s work on base erosion and profit shifting issues for developing countries and related work of the UN Committee of Experts on International Cooperation in Tax Matters?

All countries answered “yes” to this question. A number of countries said they endorsed the work being undertaken by the UN Tax Committee in this area and wanted to monitor its progress.

5. Conclusions

All respondents said that base erosion and profit shifting affected their tax revenues. Over one third said that it distorted competition between domestic, i.e. generally small, and foreign, i.e. generally large, enterprises. Some countries referenced the additional tax burden placed on other taxpayers if MNEs were avoiding tax, and the effects this could have on voluntary compliance and the development of their economies.

Transfer pricing, including the pricing of goods, excessive management fees, royalties, and research and development (R&D), was the most commonly raised base erosion and profit shifting issue. Better transfer pricing guidelines and legislation were seen as the primary tools to address this. High interest deductions on related-party debt and concerns as to excessive debt levels also featured prominently in the responses. In addition, tax havens, preferential tax regimes and treaty abuse were cited as causes of base erosion and profit shifting.

A lack of information and capacity building were other common themes. The tax 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 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 of particular concern. These were closely followed by the transfer pricing actions on intangibles (Action 8) and other high-risk transactions, including management fees (Action 10).

Finally, there was less agreement as to whether other action items not prioritized in the questionnaire are nevertheless important to developing countries. However, the avoidance of PE status (Action 7) and the digital economy (Action 1) are the two action items that were most commonly cited in response to this question.

11. OECD, *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations* (OECD 2010), International Organizations’ Documentation IBFD, also available at www.oecd.org/ctp/transfer-pricing/transfer-pricing-guidelines.htm.