

**TAX EXECUTIVES INSTITUTE-SAN JOSE STATE UNIVERSITY
HIGH TECH TAX INSTITUTE**

Practical Consequences of BEPS

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BEPS Overview

- The OECD presented a BEPS (base erosion and profit shifting) action plan at the G-20 finance ministers' July 19, 2013 meeting in Moscow. The BEPS project identified 15 specific actions.
- BEPS is the most ambitious international tax project in history.
- The goal of BEPS is for countries to agree to a unified plan for international tax.
- BEPS represents an attempt to eliminate double nontaxation or so-called “stateless income.”
- The BEPS project is intended to lay the foundations of a modern international tax framework under which profits will be taxed where economic activity and value creation occurs.

BEPS Final Reports

- The final reports were released on October 5, 2015. On October 9, the G-20 approved the OECD recommended changes to the international tax rules and to implementation plans.
- All G-20 and OECD countries worked on equal footing and the European Commission and developing countries were involved throughout the project.
- BEPS is designed to be implemented via changes in domestic law and practices, and via treaty provisions.
- Members of Congress have stated that U.S. tax policy will not be constrained by BEPS concessions to which Congress has not agreed.

BEPS Action Items

- (1) address the challenges of the digital economy;
- (2) neutralize the effects of hybrid mismatch arrangements;
- (3) strengthen the controlled foreign company rules;
- (4) limit base erosion via interest deductions and other financial payments;
- (5) counter harmful tax practices more effectively, taking into account transparency and substance;
- (6) prevent treaty abuse;
- (7) prevent the artificial avoidance of permanent establishment status;
- (8, 9, and 10) assure that transfer pricing outcomes are in line with value creation regarding intangibles, risks and capital, and other high-risk transactions;
- (11) establish methodologies to collect and analyze data on BEPS and the actions to address it;
- (12) require taxpayers to disclose their aggressive tax planning arrangements;
- (13) reexamine transfer pricing documentation;
- (14) make dispute resolution mechanisms more effective;
- (15) develop a multilateral instrument to enable interested countries to implement measures developed in the course of the BEPS work and amend bilateral tax treaties.

BEPS Implementation

- BEPS measures range from new minimum standards that countries have agreed to adopt immediately to suggested revisions to existing standards.
- Minimum standards tackle issues in cases where no action by some countries would create negative spill overs.
- All OECD and G20 countries committed to consistent implementation in the areas of:
 - Preventing Treaty Shopping,
 - Country-by-Country Reporting,
 - Fighting Harmful Tax Practices, and
 - Improving Dispute Resolution.
- In other areas, countries have agreed on a general tax policy direction and best practice guidance.

Action Item 2: Hybrids

- Action 2 is intended to neutralize the effects of hybrid mismatch arrangements.
- Hybrid arrangements are arrangements that exploit the different tax treatment of an entity or an instrument in different countries.
 - A classic example that many technology companies have used is Luxembourg CPECs, an instrument which is treated as debt for Luxembourg purposes but equity for U.S. tax purposes.
- The BEPS recommendations do not attempt to resolve competing characterizations.
- The hybrid mismatch arrangement BEPS measure is a best practices recommendation.

Action Item 3: CFC Rules

- The goal of Action 3 is to strengthen controlled foreign corporation (CFC) rules.
- The report sets out building blocks for effective CFC rules.
- CFC rules are very different in countries that use a worldwide system of taxation, like the U.S., versus a territorial system like most of the rest of the world.
- The Action 3 report provides best practice guidance.

Action Item 4: Interest

- Action 4 focuses on base erosion via interest deductions.
- The report analyzes several best practices and then provides a suggested approach based on a fixed ratio rule.
- Many countries already have thin capitalization or similar rules to prevent base erosion. In the U.S. interest stripping is limited under § 163(j).
 - Congressional action would be required to change Section 163(j) and a change in the statute is unlikely to be done any time soon.
- The Action 4 report provides best practice guidance on general tax planning direction.

Action Item 5: Harmful Tax Practices

- Action 5 is the only action plan focusing on competition among countries to improve their economies and attract foreign investments by granting tax benefits.
- The final report mandates a compulsory spontaneous exchange of rulings related to:
 - preferential regimes;
 - cross-border unilateral advance pricing agreements or other unilateral transfer pricing rulings;
 - a downward adjustment to profits;
 - permanent establishments; and
 - conduits.
- For countries that have the necessary legal basis in place, an exchange of information will take place starting April 1, 2016 for future rulings. The exchange of certain past rulings will need to be completed by December 31, 2016.
- Action 5 is a minimum standard that all countries participating in BEPS have agreed to implement.

Action Item 6: Treaty Abuse

- Action 6 addresses treaty shopping.
- Treaty abuse is a minimum standard that all countries participating in BEPS have agreed to implement.
- The report allows some flexibility in implementation.
- Most treaties generally already have antiavoidance rules to prevent treaty shopping.
- The U.S.'s limitation on benefit treaty provision addresses treaty shopping.
- Treaty abuse is a minimum standard that all countries participating in BEPS have agreed to implement.

Action Item 11: Analyzing BEPS Data

- Action 11 deals with analyzing data on BEPS.
- When the BEPS project started, the OECD released a report regarding the magnitude of BEPS and concluded that with the data currently available, it is difficult to reach solid conclusions about how much BEPS actually occurs.
- The OECD estimates in the Final Report that BEPS may result in corporate tax losses of 4-10%, for 2014 that equates to \$100-\$240 billion.
- The Final Report admits that the data is not comprehensive and does not adequately isolate BEPS from other economic factors.

Action Item 14: Dispute Resolution

- Dispute resolution is a minimum BEPS standard.
- The minimum standard will:
 - Ensure that treaty obligations related to the mutual agreement procedure are fully implemented in good faith and that mutual agreement cases are resolved in a timely manner;
 - Ensure the implementation of administrative processes that promote the timely resolution of treaty-related disputes; and
 - Ensure that taxpayers can access the mutual agreement procedures when eligible.
- The implementation of the minimum standard will be monitored using a detailed methodology that will be developed in 2016.
- In addition to the minimum standard, twenty countries have also declared their commitment to provide for mandatory binding arbitration in tax treaties.

Action Item 15: Multilateral Instrument

- Action 15 of the BEPS project provides an analysis of the tax and public law issues related to the development of a multilateral treaty instrument.
- The U.S. initially declined to participate in the BEPS multilateral treaty project but the U.S. has recently stated that it will participate mainly to advocate for mandatory binding arbitration.

OECD BEPS Action 7

Artificial Avoidance of PEs

Changes in the Final Report

- The October 2015 final report is an improvement over the May 2014 discussion draft, but does loosen the existing PE definition.
- Does not propose industry-specific PE standards, e.g., for e-commerce or insurance
- Guidance concerning the attribution of profits to PEs related to changes implemented via Action 7 will be carried on after September 2015, with necessary guidance to be issued before the end of 2016.

Three issues specifically addressed by proposed changes to Article 5 and Commentary:

Dependent Agent Standard (5.5)

- Targets commissionaires and similar strategies
- Replaces “conclusion of contracts” and “in the name of” with looser standards
- Independent agent exception cannot apply where agent acts exclusively or almost exclusively for connected persons

Preparatory and Auxiliary Activities (5.4)

- Addresses concern over artificial avoidance of PE status through use of the specific activity exemptions for preparatory and auxiliary activities
- Options of (a) subjecting all specific activity exemptions to an overall prep & aux condition, or (b) retaining existing exemptions so long as the “anti-fragmentation rule” is adopted (grouping activities of connected enterprises)

Splitting Contracts (PPT rule)

- Addresses installation, construction and service PEs
- No specific rule in Article 5; instead relies on proposed principal purpose test
- New example in Commentary

OECD BEPS Action 7

New permanent establishment definition under Article 5, Para 5

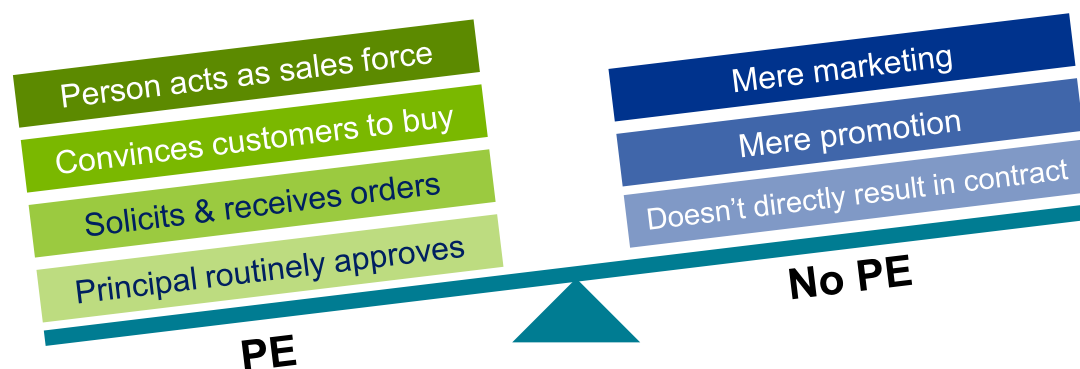
*Notwithstanding the provisions of paragraphs 1 and 2 but subject to the provisions of paragraph 6, where a person is acting in a Contracting State on behalf of an enterprise and, in doing so, **habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise , and these contracts are***

a) in the name of the enterprise, or

*b) **for the transfer of the ownership of, or for the granting of the right to use, property owned by that enterprise or that the enterprise has the right to use, or***

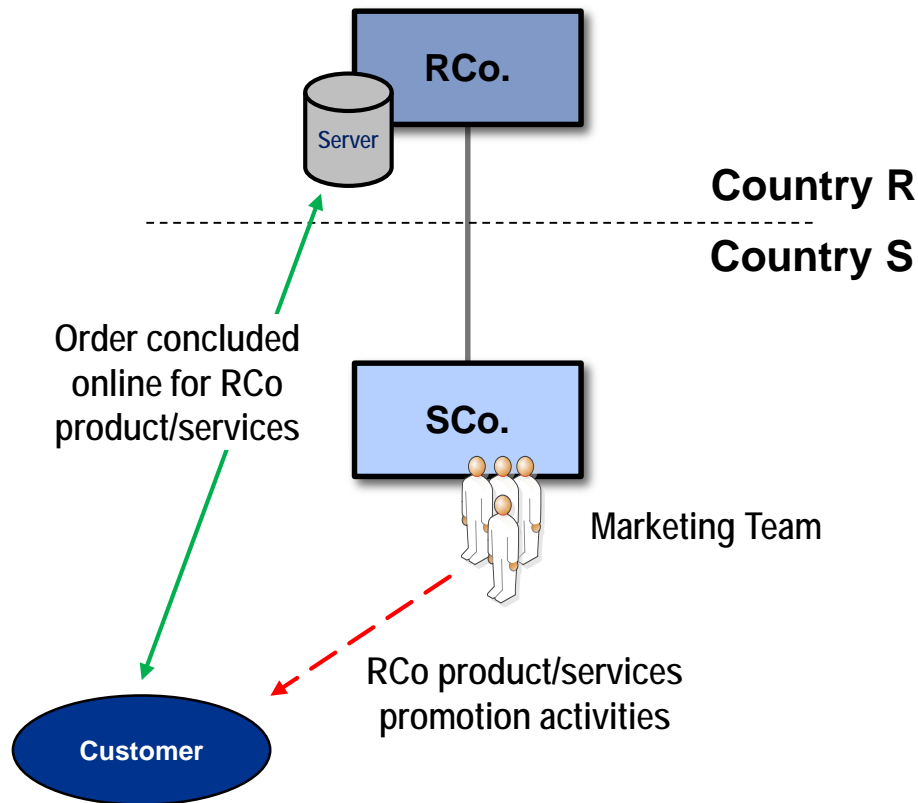
*c) **for the provision of services by that enterprise,***

that enterprise shall be deemed to have a permanent establishment in that State in respect of any activities which that person undertakes [unless such activities would be exempt under paragraph 4]. (convinces customers to buy,



OECD BEPS Action 7

Art 5.5(b) Illustration (para 32.6): Customer-Facing PE



Description

- RCO (State R resident), distributes products and services through its websites. RCO owns SCO (State S resident)
- SCO's employees promote RCO's products and services. Their remuneration is partially based on revenues derived by RCO from holders of S's accounts
- When an account holder agrees to purchase goods promoted by an SCO employee, the employee indicates the price that will be payable and that the contract must be concluded online with RCO, and explains the standard terms of RCO's contracts. The employee cannot modify these terms

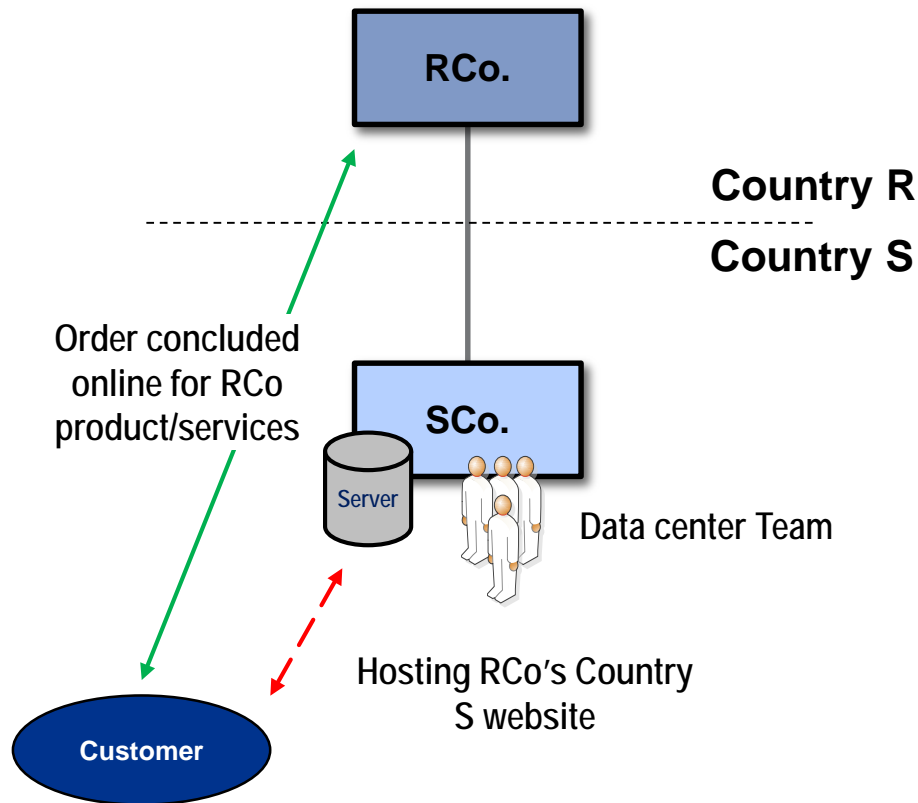
Results:

- SCO's employees play the principal role leading to the conclusion of the contracts routinely approved by RCO without modification

"The fact that SCO's employees cannot vary the terms of the contracts does not mean that the conclusion of the contracts is not the direct result of the activities that they perform on behalf of the enterprise, convincing the account holder to accept these standard terms being the crucial element leading to the conclusion of the contracts between the account holder and RCO." *Proposed commentary on Art 5.5 (Para 32.6)*

OECD BEPS Action 7

Digital Economy business model - Similar to paragraph 32.6 example?



Description

- RCo (State R resident), distributes digital products and services through its websites. SCo manages the Country S data center hosting RCo's Country S website
- Customer purchases are at standard terms contracted on-line through RCo's website

Considerations:

- Will SCo's activities cause RCo to have a PE under Art 5.5?

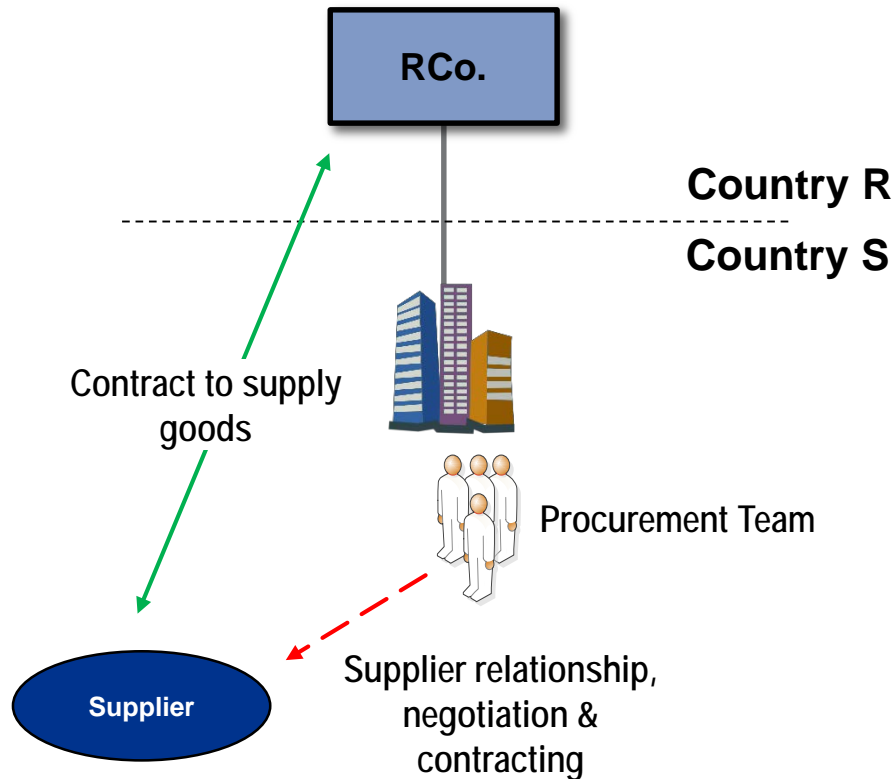
“Despite [increased DE supply chain mobility], in many cases large MNEs will indeed have a taxable presence in the country where their customers are located. . . . there are often compelling reasons for businesses to ensure that core resources are placed as close as possible to key markets. . . . It may be because minimising latency is essential in certain types of business, or because in certain industries regulatory constraints limit choices about where to locate key infrastructure, capital, and personnel.” *Action 1 Final Report (Para 255)*

“[Dependent] persons whose activities may create a PE for the enterprise may be either individuals or companies. . . .” *Prop commentary on Art 5.5 (Para 32)*

- SCo's role in presenting standard terms is limited to maintaining the servers hosting RCo's website.
 - Who undertakes “the principal role leading to the conclusion of contracts”?
 - Even if SCo were deemed to “play the principal role”, how could DC operations be considered more than prep & aux?

OECD BEPS Action 7

Art 5.5(b) Illustration (para 32.2): Supplier-Facing PE



Description

RCO sources products from Country S that it then distributes from Country R. RCO's Country S employees are experienced buyers and negotiate and enter into supply contracts for RCO

Results

- RCO has a Country S PE. “. . . although [RCO's Country S purchasing activity] is an activity covered by subparagraph d) [(a specified exception to a fixed place of business PE), the exception] does not apply and the office therefore constitutes a PE because the purchasing functions form an essential and significant part of RCO's overall activity.” *Proposed commentary on Art 5.4 (Para 22.5)*

Queries

1. What if Country S employees were employed by SCO (rather than RCO)? Could RCO have a dependent agent PE under Art 5.5?

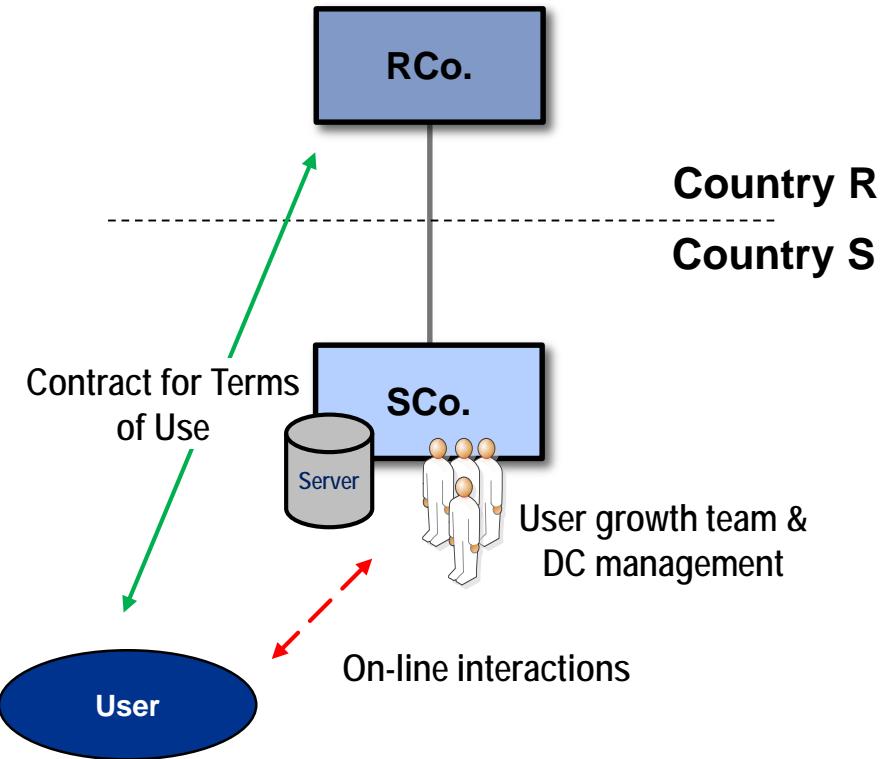
“Where, for example, a person acts solely as a buying agent for an enterprise and, in doing so, habitually concludes purchase contracts in the name of that enterprise, paragraph 5 will not apply [i.e., no PE] even if that person is not independent of the enterprise as long as such activities are preparatory or auxiliary (see paragraph 22.5 above).” *Proposed commentary on Art 5.5 (Para 32.2)*

2. Does the scope of Art. 5.5 include 'buy-side' contracts?

“The contracts referred to in Art 5.5 cover contracts relating to operations which constitute the business proper of the enterprise.” *Proposed commentary on Art 5.5 (Para 33)*

OECD BEPS Action 7

2-sided Digital Economy business model - Similar to paragraph 32.2?



Description

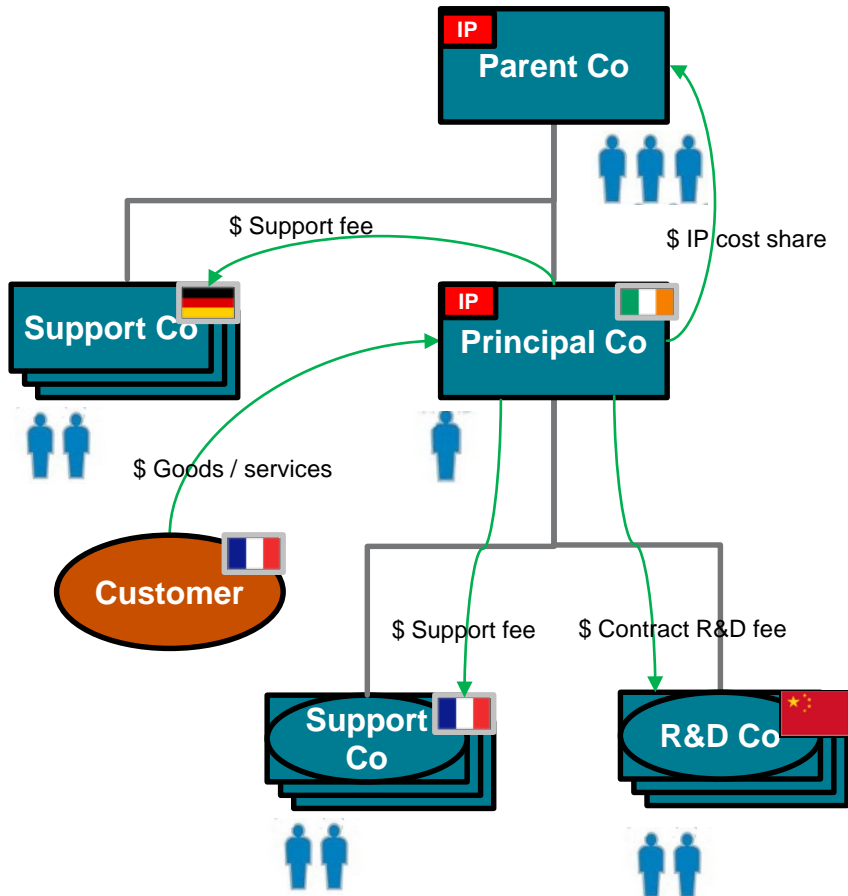
RCO has a significant number of Monthly Active Users (MAU) in Country S. Users provide personal data to RCO in exchange for the free use of RCO's websites. User data enhances the value of RCO's digital products & services sold to Customers.

SCO manages the data center that hosts RCO's websites. The SCO DC does not accept Customer orders for goods or services. SCO also promotes the growth of RCO's MAUs in Country S

Considerations

- Could SCO's role in MAU promotion and DC hosting cause RCO to have a PE?
- Is a User TOU contract the type of contract covered by Art 5.5?
- **"The contracts referred to in Art 5.5 cover contracts relating to operations which constitute the business proper of the enterprise."** *Proposed commentary on Art 5.5 (Para 33)*
- Who undertakes "the principal role leading to the conclusion of [the TOU] contracts"?
- Are User growth activities more than prep & aux?

Regional principal company model



Principal Co (low-taxed) sells products / services to customers outside Parent Co jurisdiction

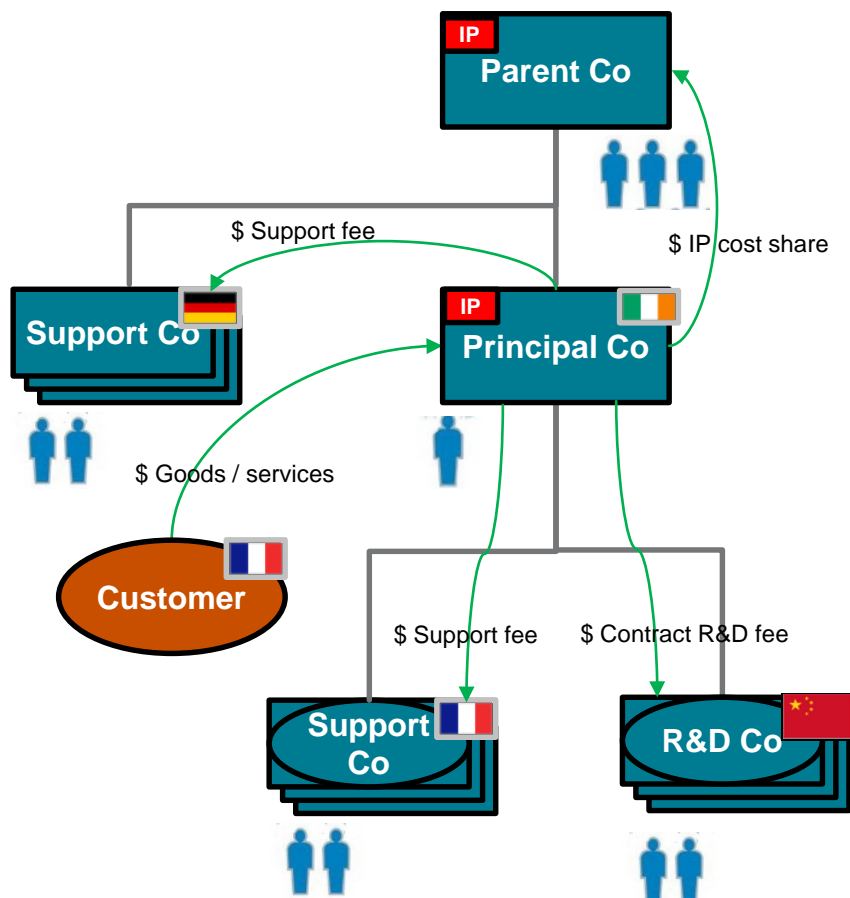
Parent Co – 5,000 employees. CCA with Principal Co for joint development of IP. Legal owner of IP (technology & brand). Majority of R&D workforce. Oversight of foreign R&D activity. Shared (with Principal Co) oversight of 3P contract manufacturers. *TP: IP development shared “at cost” under CCA.*

Principal Co – 150 employees. CCA with Parent Co for joint development of IP. Approves R&D budget. Concludes customer contracts. Shared (with Parent Co) oversight of 3P contract manufacturers. Oversight of Support Cos (customer service, marketing and promotion). Strategic decision making for foreign markets (business strategy, marketing). *TP: Support and R&D affiliates hold limited risk. Residual profit allocated to Principal Co.*

Support Cos – 2,500 marketing & support employees. Responsible for customer relationships. Presents standard terms. Conducts all customer support. *TP: “cost +”.*

R&D Cos – 150 employees. Highly qualified research engineers. Performs research under direction of Parent Co. *TP: “cost +”.*

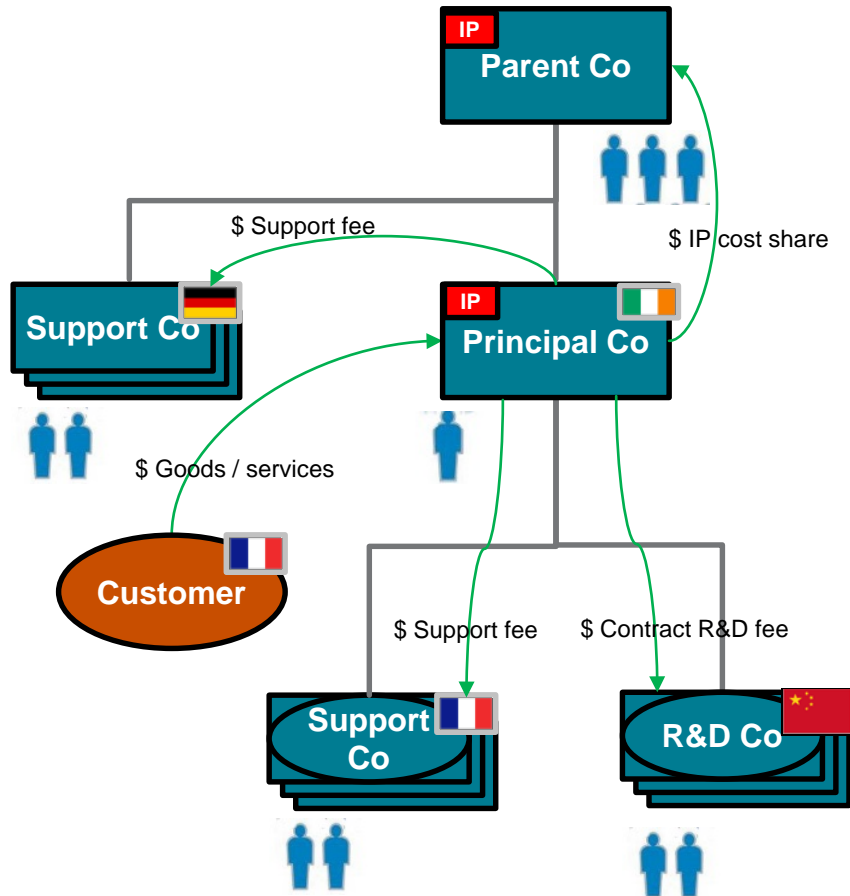
Regional principal company model: Issues



BEPS Considerations:

1. **Harmful Tax Practices (Action 5)** – Does Principal Co benefit from a potentially harmful regime?
2. **Treaty Abuse (Action 6)** – A portion of Customer payments are considered ‘technical services’ in some jurisdictions, subject to WHT absent treaty.
 - a) Any concerns that reduced treaty WHT rates would be disallowed?
3. **Permanent Establishment (Action 7)** – Support Cos are ‘NOT’ commissionaires.
 - a) If Principal Co has a PE, how will the profit attributable to the PE be determined?

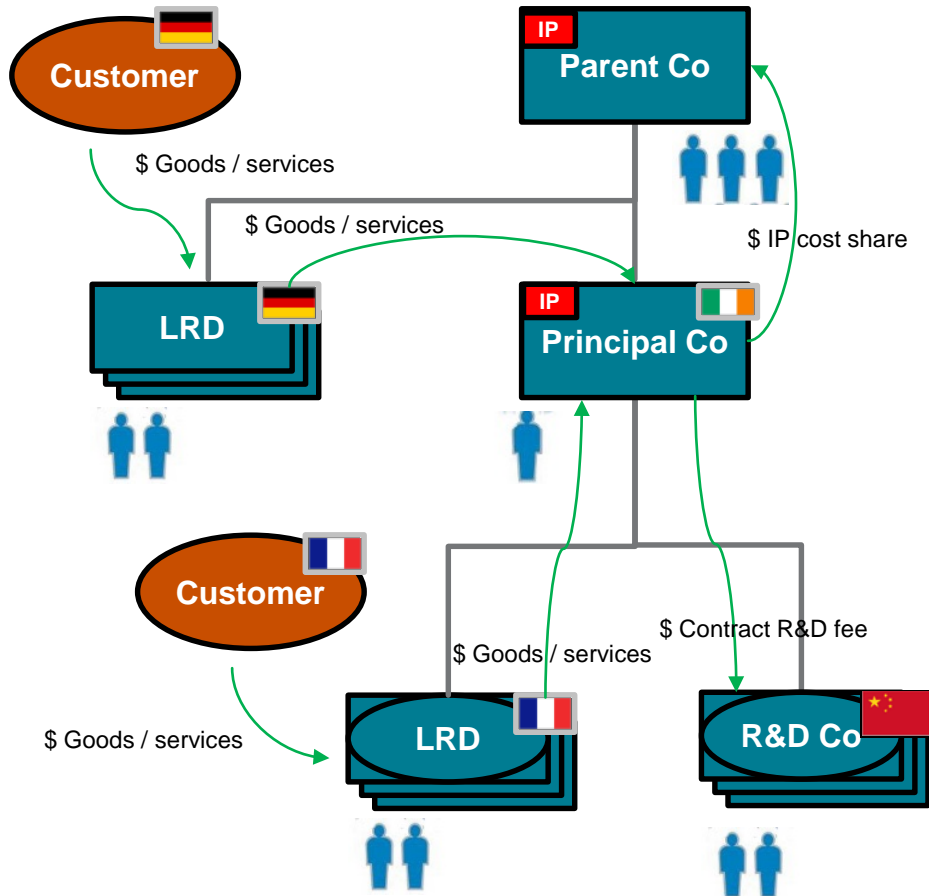
Regional principal company model: Issues (Cont.)



BEPS Considerations:

4. **Transfer Pricing (Actions 8-10) – Principal Co earns a high operating margin through one-sided TP methods**
 - a) **What are the TP risks with respect to the Support and Contract R&D fees?**
 - b) **What substance should be at Principal Co?**
5. **Disclosure of Aggressive Arrangements (Action 11)**
 - a) **Likelihood of this structure reported as an aggressive arrangement?**

Limited risk distributor (LRD) model



LRDs sell products / services to customers outside Parent Co jurisdiction

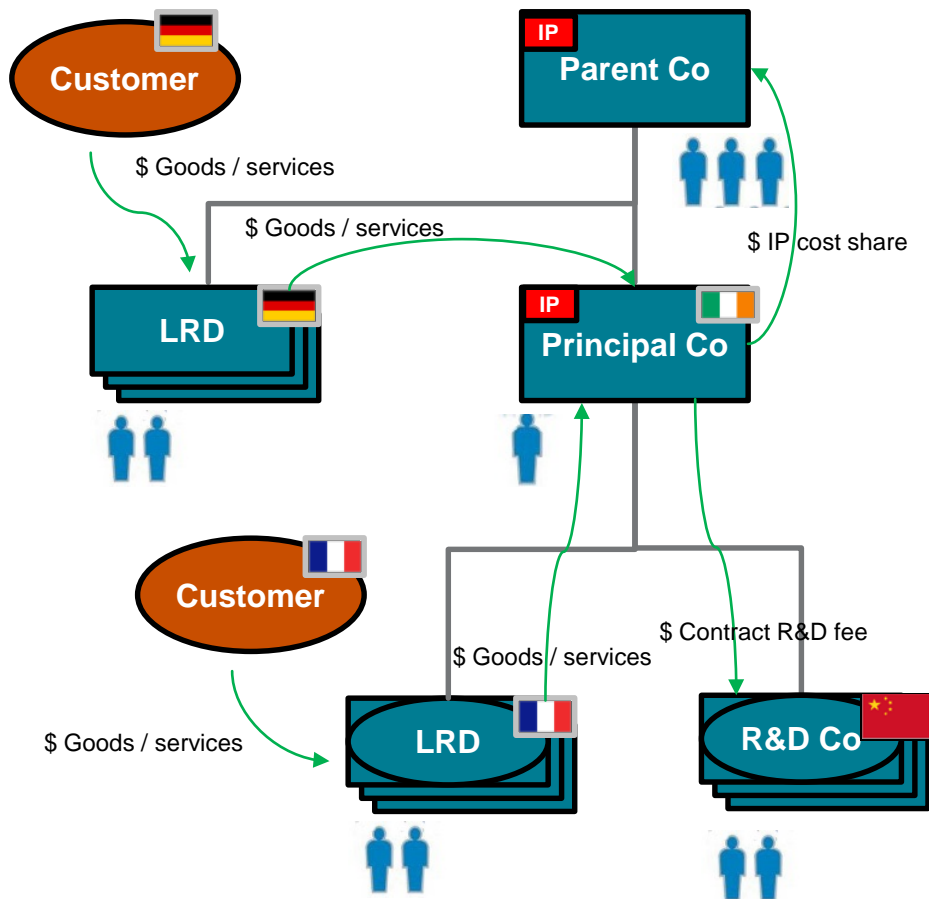
Parent Co – 5,000 employees. CCA with Principal Co for joint development of IP. Legal owner of IP (technology & brand). Majority of R&D workforce. Oversight of foreign R&D activity. Shared (with Principal Co) oversight of 3P contract manufacturers. *TP: IP development shared “at cost” under CCA.*

Principal Co – 150 employees. CCA with Parent Co for joint development of IP. Approves R&D budget. Shared (with Parent Co) oversight of 3P contract manufacturers. Strategic decision making for foreign markets (business strategy, marketing). *TP: LRD and R&D affiliates hold limited risk. Residual profit allocated to Principal Co.*

Limited Risk Distributors (“LRD”)—2,500 employees. Concludes customer contracts. Responsible for customer relationships. Conducts all customer support. *TP: TNMM.*

R&D Cos – 150 employees. Highly qualified research engineers. Performs research under direction of Parent Co. *TP: “cost +”.*

Limited risk distributor model: Issues



BEPS Considerations:

2. **Treaty Abuse (Action 6)** – Cross-border payments shifted to related parties
3. **Permanent Establishment (Action 7)** – Trade off of PE concerns for TP considerations
 - a) How do special measures such as UK DPT and Australia MAAL influence the business model?
4. **Transfer Pricing (Actions 8-10)** – Principal Co earns a high operating margin
 - a) What are the TP risks with respect to the LRD and Contract R&D fees?
 - b) If LRDs control more risk than contractually allocated, how will this gap be reconciled?
4. **Other considerations** –
 - a) Subpart F (revenue characterization, minimum tax, 954(d)(1), 954(d)(2), 954(e))
 - b) Operational matters (transfer pricing automation, change in VAT responsibilities and invoicing requirements, sales team change management)

Overview of China's Attitude on BEPS Issues

More Aggressive Enforcement on Anti-Avoidance

Year	Tax Revenue from Anti-Avoidance (Billion RMB)	Increased Compared with 2007
2007	1	0%
2008	1.2	20%
2009	2.1	110%
2010	10.27	927%
2011	23.9	2290%
2012	34.6	3360%
2013	46.9	4590%
2014	<u>52.3</u>	5130%

TP Audits in China

- TP audits statistics in 2014
 - Number of audit cases: 257
 - Tax collected: RMB7.9 billion (US\$1.3 billion)
 - 20 cases of more than RMB100 million
- TP audits scale remains small
 - 23778 FIEs were established during the year of 2014
- However, TP now is in the spotlight within SAT
- Statute of Limitations (SOL) for TP cases is 10 years
- Fast track process in some localities

Measures Introduced in China to Combat BEPS

- General Anti-Avoidance Procedural Guidance (SAT Order 32, issued on Dec. 2014)
- Expansion of indirect share transfer rules to cover indirect property transfers (Bulletin 7, issued on Feb. 2015)
- Base-Eroding Payment Rules (Bulletin 16, issued on Mar. 2015)
- Proposed Transfer Pricing Regulation released on Sept. 17, 2015

China's Planned Actions to Combat BEPS

- Domestic legislation
 - Revise the Tax Collection and Administration Law: 2016
 - Revise China's transfer pricing rules (Circular 2): 2015
 - Revise China's CFC rules: 2015
 - Enact anti-hybrid mismatch rules: 2016
 - Enact anti-treaty abuse rules: 2016
- IT system upgraded to support MNC's profit range development
- Anti-tax avoidance and bilateral treaty negotiations
- Automatic information exchange with more than 45 countries by the end of 2018
- Participation in multilateral coordination: 2016



Revised Transfer Pricing Rules

- Country-by-country reporting
- New documentation requirements
- New transfer pricing methods
- Location savings and market premium
- Special chapter for intangibles
- Special chapter for intragroup services
- Secondary adjustment
- Spill-over to other taxes?

CbC Reporting

Consistent with the OECD Proposal

- Three-tiered approach – China will adopt a standardized approach to transfer pricing documentation with a three-tier structure consisting of:
 - a **master file** containing standardized information relevant for all MNE group members;
 - a **local file** referring specifically to material transactions of the local taxpayer; and
 - a **country-by-country report** containing information on global allocation of MNE's income, taxes, other economic indicators.

Master File and Local File

- Reporting entity:
 - PRC entities have a related sale-purchase revenue of at least RMB200 (US\$33) million or other related transaction revenue of at least RMB40 (US\$6.5) million
- Should be prepared by May 31 of the following year
- Constitute parts of the transfer pricing documentation

CbC Reporting Obligation

- CbC report should be submitted as part of the controlled transaction filing along with the enterprise income tax annual filings for Chinese MNEs
- Reporting entities:
 - The Chinese ultimate controlled enterprise of the group if the group's consolidated income for the last fiscal year exceeds RMB 5 billion;
 - The ultimate parent is not in China but the Chinese entity has been designated as the reporting entity for the group.

CbC Reporting Obligation

- If the group's ultimate parent is a foreign company, and according to the rules of its jurisdiction it shall prepare CbCR, and the local entities in China are in the scope of the CbCR, the China tax authorities can request the local entities of MNES to provide CbCR if:
 - The group's ultimate parent did not prepare, nor has it designated another member of the group to prepare CbCR, or
 - Although the CbCR has been prepared, but the recipient jurisdiction did not sign CA agreement to exchange such CbCR, or
 - China tax authorities cannot get the CbCR notwithstanding the above.

New Documentation Requirements

Multi-Layer Analysis in Local File

- Transaction level
- Entity level
- Value chain analysis

Special-Purpose Documentations

- Special-purpose documentation for services
- Special-purpose documentation for CSA
- Special-purpose documentation for thin-capitalization

New Transfer Pricing Methods

Value Contribution Allocation Method

- In essence, it is global formulary apportionment method
 - Allocate profits based on factors such as assets, costs, expenses, sales, number of employees etc.
- Tax authorities can use value contribution allocation method where
 - No comparables available
 - Combined profits can reasonably determined
 - Contribution of value creation factors can be reasonably determined

Valuation methods

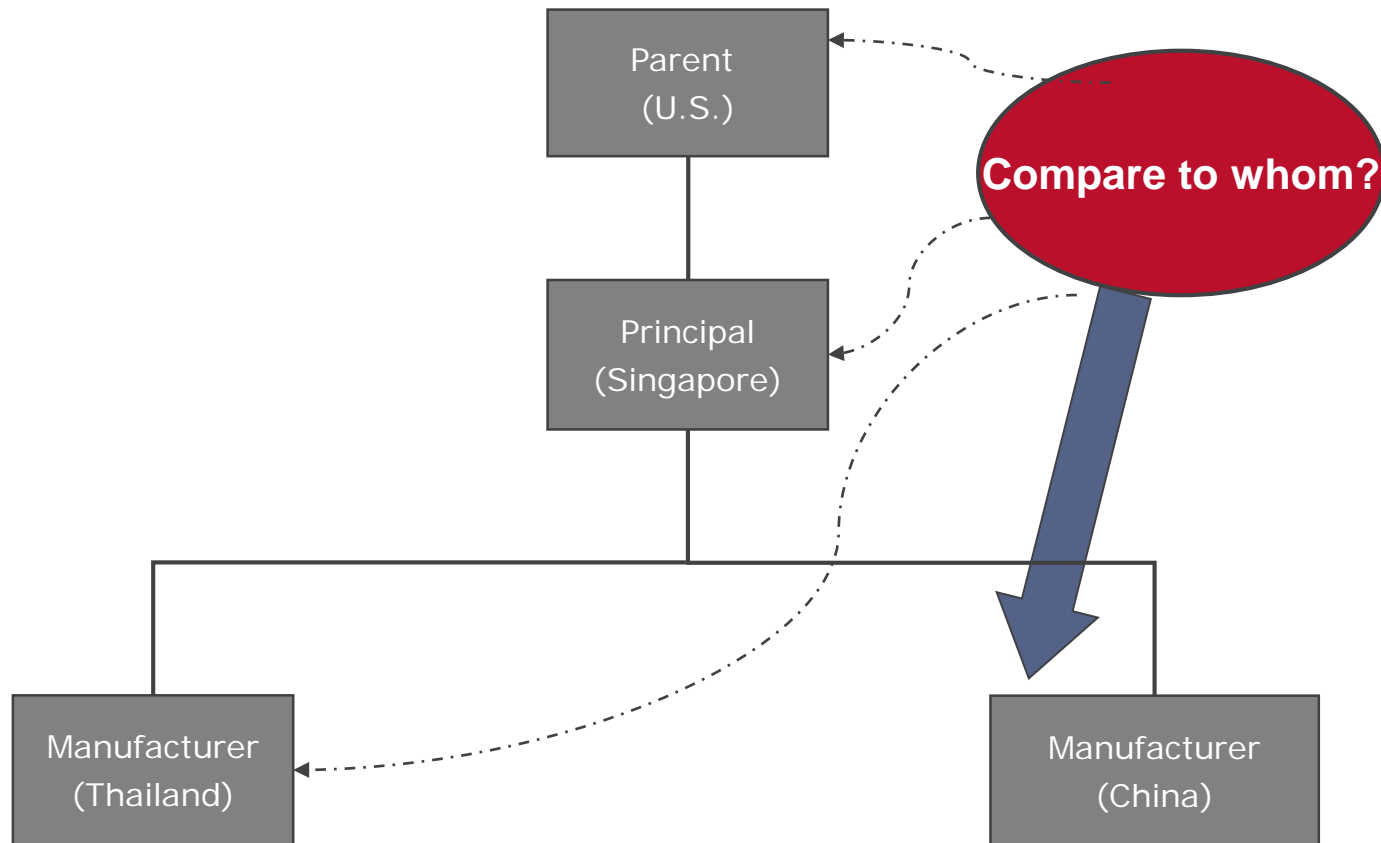
- Valuation techniques
 - Cost method
 - Income method
 - Market method

Location Specific Advantages

Location Specific Advantages (LSAs)

- Location specific advantages
 - Location savings (supply side)
 - Market premium (demand side)
- Tax authorities are required to identify and determine whether LSAs (if any) generate additional profits. If so, tax authorities are required to allocate the profits arising from the LSA using reasonable methods.

China : Quantification of LSA



China : Quantification of LSA (cont.)

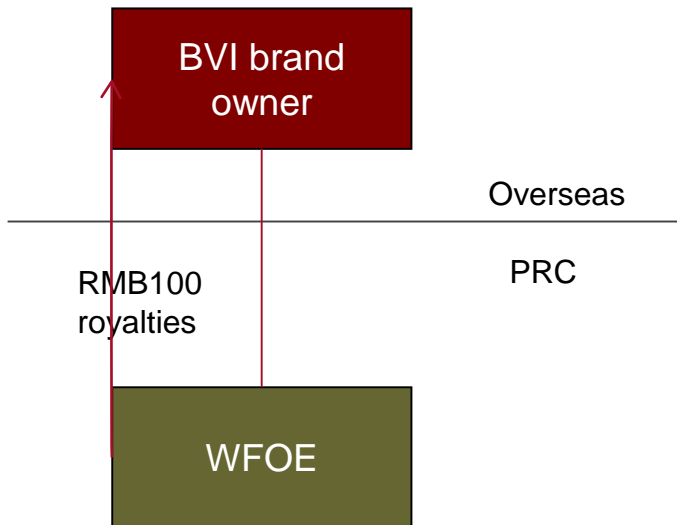
- Difficult to consistently applying the LSAs
- Use LSAs as intangibles to counter-balance IPs in arguments for profit split
- If there is no business restructuring, how to get cost information?
- Should the result be different if there is no business restructuring?

Special Chapter for Intangibles

Special Chapter for Intangibles

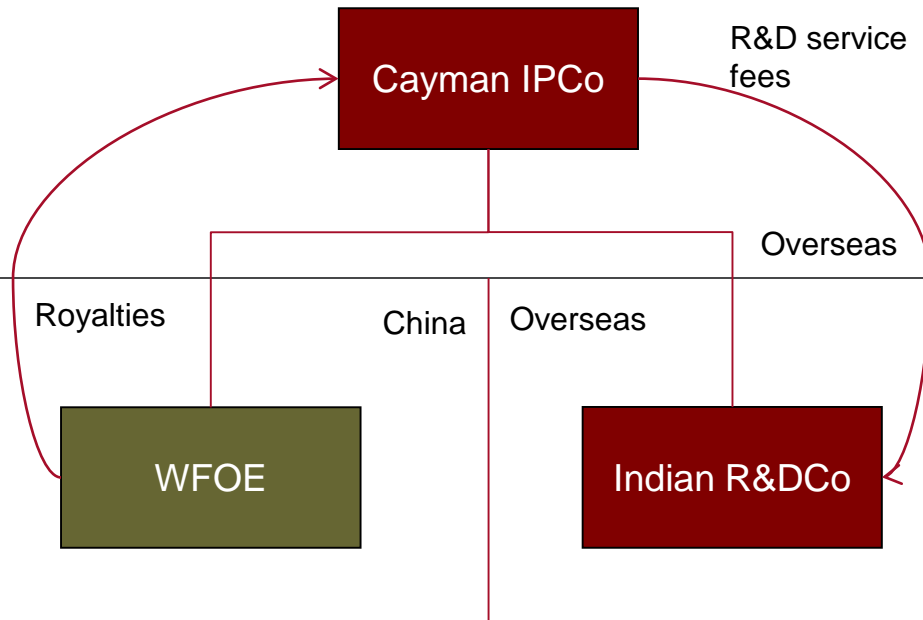
- Four methods are allowed where intangibles are involved:
 - CUT
 - Profit Split
 - Value Contribution Allocation
 - Valuation
- More profit split and global formulary apportionment for profits arising from intangibles
- Legal ownership vs. Economic ownership
- Sole funding only receives an return to capital

The Chengdu Case: Brand Value



- The WFOE had contributed significantly to the development of the foreign brand in China
- Tax authority took the view that WFOE should not be paying a large royalty to the BVI brand owner
- Most of royalties payments were denied deductions
- WFOE: economic owner of the brand?
- Tax bill: RMB23 million

Are Royalties Deductible if WFOE is not Economic Owner?



- BVI is a pure legal owner and does not contribute to the value creation of the IP
- India is the economic owner and performs all functions related to the IP; R&D service fees are not sufficiently compensated
- Royalties paid to BVI are arm's length
- Are royalties deductible at WFOE? Or China is going to tax what “should” be taxed in India?

Special Chapter for Services

Benefit Tests for Services

- Benefit tests: PoP
- Negative lists
 - Duplicative
 - Shareholder activities
 - Incidental
 - Remunerated by other means
 - Irrelevant
 - Others

Secondary Adjustment

Secondary Adjustment

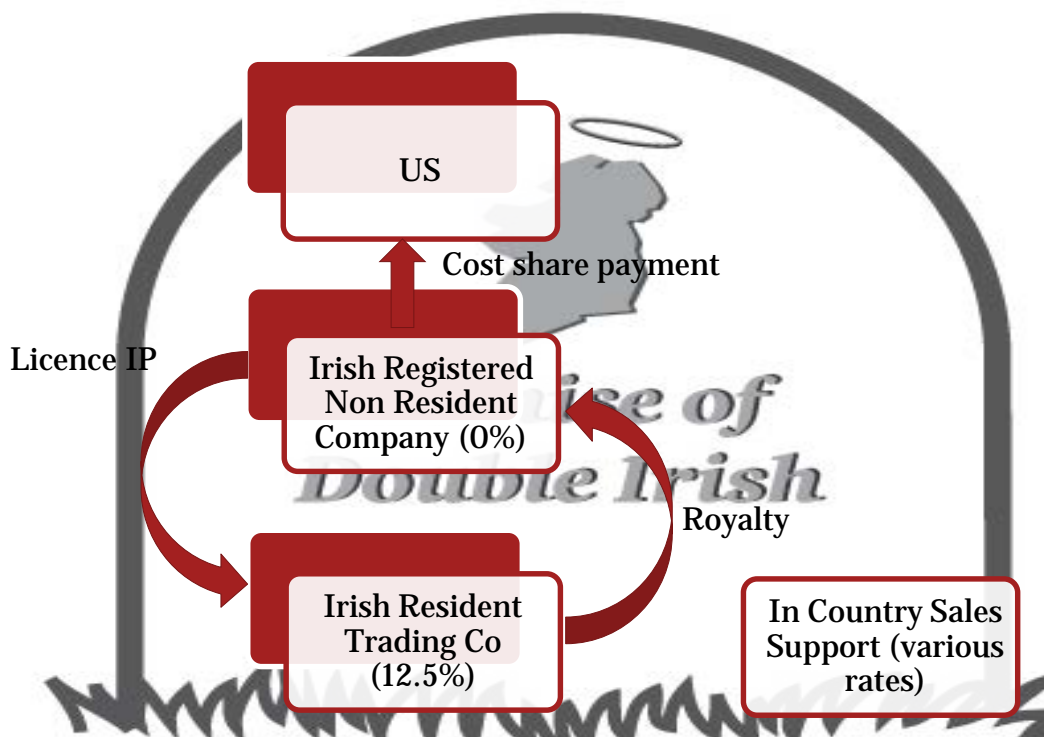
- Taxpayers are required to align their accounts with the transfer pricing adjustment
- Need to remit the cash to the affected Chinese entities within required time period
- If not, secondary adjustment based on deemed dividend distribution

Spill-Over to Other Taxes

Requirement to Align Other Taxes with Transfer Pricing Adjustment

- Taxpayers are required to make adjustment for other taxes after they pay EIT due to adjustment
- However, special tax adjustment is only authorized under the EIT law
- High compliance cost for taxpayers

Did BEPS “kill” the double Irish (the west coast structure of choice)??



How did it work?

- “Secret sauce” is WHT regime, not country of incorporation
- Increasing importance of IP in value chain facilitates low overall effective rate

But BEPS doesn’t target WHT?

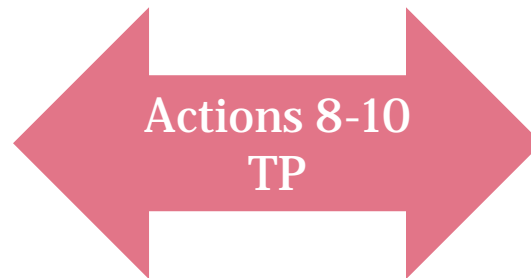
- Ireland jumped before it was pushed – grandfathered until 31 December 2020.
- But really it’s all about TP.....

Understanding the meaning and importance of 'substance'

Intellectual Property



Operating model

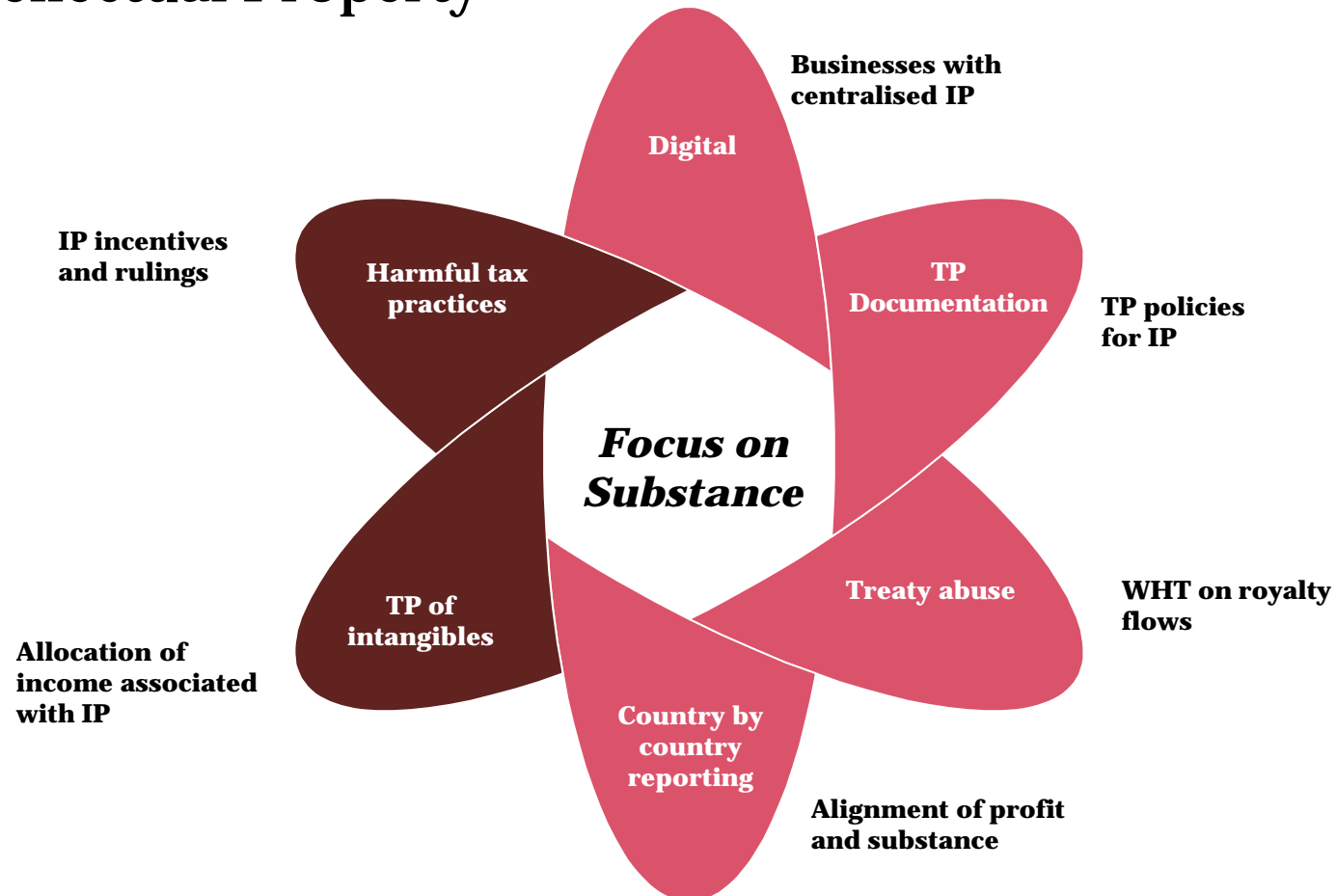


Actions 8-10
TP

Understanding the meaning and importance of 'substance'



Intellectual Property



Understanding the meaning and importance of 'substance'



Impact of BEPS – Transfer pricing on intangibles – Key themes

Definitional aspects – Ch 6

- Intangibles continue to be broadly split between 'marketing' and 'trading', although it is made clear that the classification of an intangible will not affect the level of transfer pricing analysis required.

Legal ownership – Ch 6

- Clarification that legal ownership by itself does not confer any right to ultimately retain any intangible related return.
- Similarly, funding intangible development in isolation is likely to result in a lending level of return as opposed to return on equity.

Dual-sided analysis – Ch 6

- A functional analysis should be performed in order to understand how an intangible interacts with an MNE's other functions, assets and risks, thus a one-sided analysis may not reliably evaluate a transaction involving an intangible.

Marketing spend – Ch 6

- Consideration should be paid to the possibility that a marketer/distributor could enhance the value of an intangible. In such cases, the nature of the costs and the substance of the (future) rights of the relevant party should be reviewed.

Understanding the meaning and importance of ‘substance’



Impact of BEPS – TP on intangibles (continued) – Key areas of focus

Group synergies – Ch 1

- Remuneration only appropriate where there is ‘deliberate concerted group action’ providing material advantages. Benefits should be allocated based on contribution towards creation of the synergy

Assembled workforce – Ch 1

- Transfers/Secondments shouldn’t necessarily require separate compensation, though any associated know-how and time and expense savings (or any detrimental effects) should be reflected in the arm’s length price

Location savings – Ch 1

- Not an intangible, but pricing where they exist should be based on comparable entities and transactions in the local market. Where such comparables cannot be identified, comparability adjustments may be required

Group name – Ch 6

- In general no payment should be made merely for use of group name. Any consideration paid should reflect the functions, assets and risks borne by the user of the name in enhancing the value of the name in its jurisdiction

Understanding the meaning and importance of 'substance'



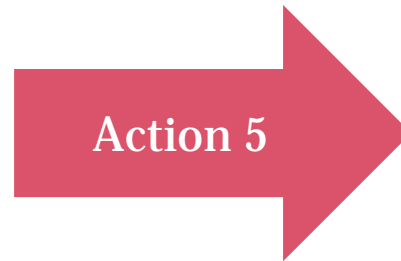
DEMPE functions are the key to residual profits

- For any business to be able to justify their right to the residual returns relating to intangibles they must be able to demonstrate that they are performing the following functions:
 - **D**evelopment
 - **E**nhancement
 - **M**aintenance
 - **P**rotection
 - **E**xploitation

What does this mean for



So are boxes the answer?



- Modified nexus is the only game in town
- If they work they are great.....but that's a big if, and in the tech world is that an improbable if?

Understanding the meaning and importance of 'substance'



Impact of BEPS – Harmful tax practices

Targeted IP regimes

Belgium	Patent income deduction
Columbia	Software regime
France	Reduced rate for licencing of IP
Hungary	IP regime for royalties and capital gains
Israel	Preferential company
Luxembourg	Partial exemption for IP rights
Portugal	Partial exemption for IP rights
Netherlands	Innovation box
Spain	Partial exemption for IP rights
Spain – Basque Country	Partial exemption for IP rights
Spain – Navara	Partial exemption for IP rights
Switzerland	Relief for new re-designed enterprises
Switzerland – Nidwalden	Licence box
Turkey	Technology development zones
United Kingdom	Patent box

Understanding the meaning and importance of 'substance'



Impact of BEPS – Harmful tax practices

- Box: New or old regime?

- New -
$$\frac{\text{Qualifying expenditures incurred to develop IP asset}}{\text{Overall expenditures incurred to develop IP asset}} \times \text{Overall income from IP asset} = \text{Income receiving tax benefits}$$

- Irish KDB – first to market

- Old regime – grandfathering and safeguards

- New entrants not allowed after 30 June 2016 (this includes new IP assets)

- Enhanced transparency for new entrants

- Related party transfers to qualify for regime will be difficult

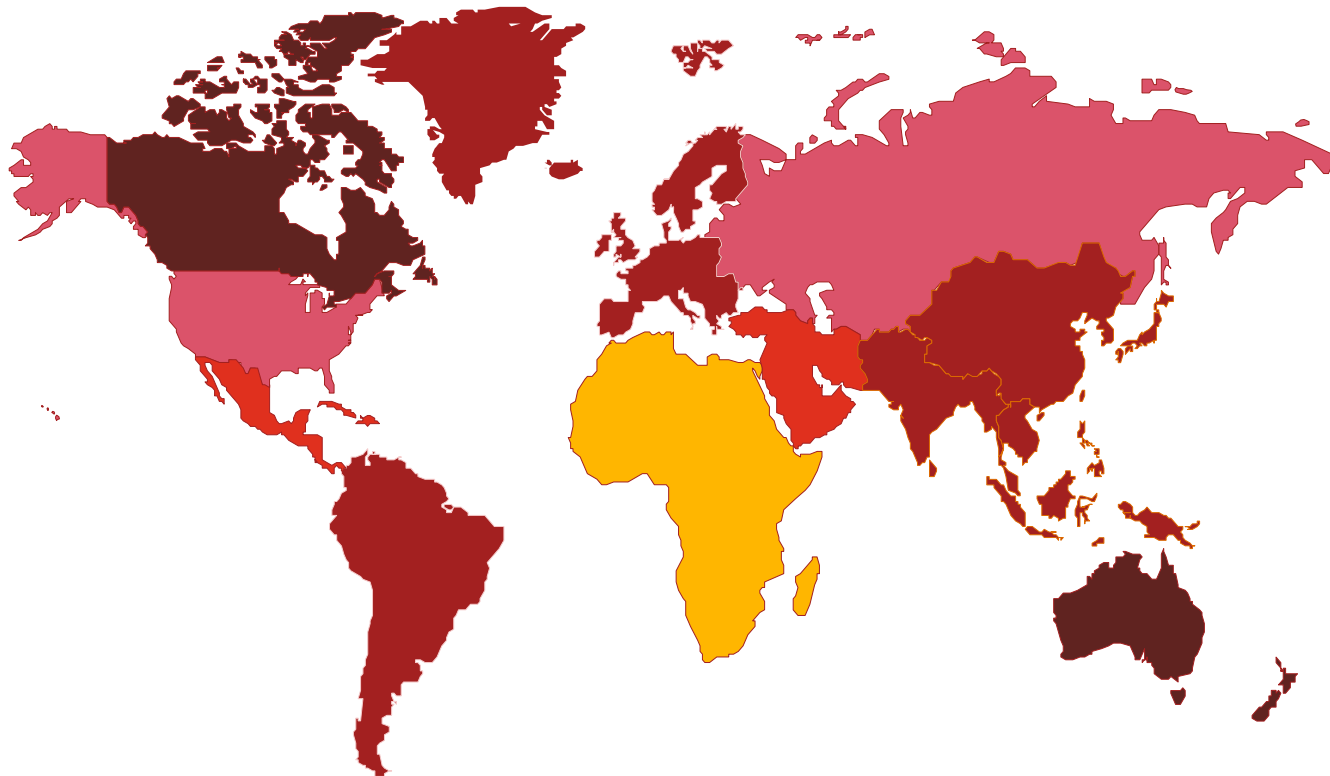
- Box: If under modified nexus

- Location of R&D activity

- History of IP (where generated, cost of acquisition, R&D etc)

- Rulings: Automatic exchange of rulings information – days of unilateral rulings and APAs are gone?

Action 13 BEPS – Country by Country Reporting



FY16

**Global
turnover of
€750m+**

**File in
country of
ultimate
parent**

Action 13 BEPS – Country by Country Reporting Challenges

Onerous data gathering

Commercially sensitive data disclosed

Revenue Authority reaction

Your CbCR message



Increased transparency is the biggest win for the OECD as it will drive change for years to come

What's the EU's position?



BEPS

- The EU were left behind and are scrambling to regain relevance by addressing BEPS.
- The EU has teeth that the OECD doesn't have....
-but on tax issues unanimity must be gained – but is using a veto likely?

CC(C)TB

- Re-launch of the CCCTB – likely to be the CCTB?
 - CCCTB – a way to shoehorn BEPS into the union
 - A draft “anti-BEPS” directive likely in the first half of 2016

State Aid

- Four cases - very political!
- Fiat & Starbucks are out – negative with recovery!
- Apple & Amazon – coming soon – negative with recovery!
- Not about rate or residence!

Where will it end?

It's all about the relativities

Havens



Thank You

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