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# Anti-BEPS Measures and Their Impact on Business Performance of Multinational Enterprises

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## Abstract

This paper discusses the harmful tax practices of multinational enterprises (MNEs) and the fight of international organizations against them. We focus on the anti-tax base erosion and profit shifting project (anti-BEPS project) of the Organisation for Economic Co-operation and Development (OECD), namely its 15 actions, which we present in the first part of the paper, using descriptive and analytical methods. In the second part, we use critical and synthetic methods to assess how the selected aspects of multinational business will be impacted with described actions. Our conclusions show that MNEs will have to adapt their business structures and plans according to new tax regulations, which will also lower their profit levels due to unavailability of established harmful tax structures for lowering their tax bases. At the same time, our results indicate that the legal approach in introducing new measures on the subject field, lead to legal uncertainty in tax matters. Due to the scope of analysed problems, it was impossible to introduce individual problems in depth; however, we provide readers with the general characteristics and goals of introduced actions that are necessary for understanding our evaluation of their impact on certain fields of international business. Our paper contributes to literature and practice, as it provides general insight into recent and important international tax law developments that enterprises will have to consider when doing business across borders.

**Keywords:** BEPS, OECD, international tax law, tax, DTC, tax planning, profit shifting, tax base erosion, corporate income tax

## Introduction

Interconnection and interaction of national economies and markets increased enormously within the last few decades. Established and traditional tax systems are put before a challenge, where the existing rules in connection to complex organizational structures of multinational enterprises (MNEs), create opportunities for tax base erosion and profit shifting (BEPS). Legislators are challenged to establish tax systems, which will enable and secure taxation of profits in the place of their creation, i.e. in the place of economic performance and value creation and thus restore the trust in fairness of taxation. Daily news provides headlines on profit allocation issues, whereby the profit, achieved by an MNE in one country, is being shifted to another country, often with the purpose of achieving favourable tax treatment of said profit and to decrease worldwide tax liability on a group level. Such actions deprive economies from taxes, which should have been collected for profits achieved on their territory. The most notorious cases have

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been related to harmful tax practices of MNEs like Google, Amazon, Facebook, Apple, etc. (i.e. the GAFA companies).

BEPS occurs when MNEs shift their profits from jurisdictions of their creation in compliance to the applicable tax laws, however usually misusing the laws or rather their legal loopholes. Such profit shifting is one of the biggest issues of international taxation and shall be treated broadly, also from macroeconomic aspect and with respect to the integrity and fairness of tax systems. The scope and tactics of MNEs go nowadays well beyond doing paper business offshore. Using differences and loopholes in tax systems is the main tool to achieve unintended tax benefits, whereby the common aim of BEPS practices is to minimise tax or even to pay zero tax in some tax jurisdictions.

Tax jurisdictions that noted BEPS of MNEs on their territory announced a determinative combat against harmful tax practices, i.e. fight against BEPS, aiming to establish tax environments that will diminish opportunities for BEPS manoeuvres. Their fight is unified under international organizations such as OECD and European Union (hereinafter "EU"). On such shortly described grounds, the OECD had in October 2015 adopted 15 actions, which shall be or are recommended to be implemented by the countries to prevent or at least limit BEPS. Out of 15 measures, only 4 are mandatory, binding the OECD and joining countries to adopt them, while other 11 measures are recommendations.

More related to the Slovenian tax system are the EU measures, prepared by the European Commission and other competent bodies, which rely on and consider strongly also the OECD anti-BEPS measures, although implementing also the other measures, which often have roots in the practice of the CJEU<sup>1</sup>. This paper, however, focuses on the 15 OECD anti-BEPS actions. It is to be emphasised that the anti-BEPS measures deal mainly with direct taxation, while indirect taxation is recognised as problematic as well, especially on the field of digital economy taxation. Nonetheless, in this article, we are dealing only with the direct and corporate taxation.

## Illegal/Legal/Immoral Tax Practices and Where Do We Find BEPS

Differentiating harmful tax practices represents one of the main issues in anti-tax avoidance and evasion legislation. Terms like tax fraud, tax evasion, tax avoidance, aggressive tax planning, have as many definitions as there are authors on the subject field. A lot of misunderstandings are caused

by inadequate translations of international documents to local languages. However, the clearest guideline is established among tax avoidance and tax evasion, the former representing actions within the legal frame, the latter being generally prohibited by the applicable law (such as reporting false income or expenses to tax authority with the aim to evade the applicable tax). Aggressive tax planning means using the advantages in technicalities of tax systems and tax system mismatches to achieve lower tax base (Cordewener, 2017, p. 61)<sup>2</sup>. From an economic point of view, legal considerations apart, harmful tax practices have similar effects, namely a reduction of revenue yields, and are based on the same desire to reduce the tax burden (Kirchler, Maciejovsky, & Schneider, 2003, p. 535).

Sandmo put harmful tax practices definitions to simpler and efficient words. He explained that tax evasion means breaching the law. When an individual omits to report an income, which should have been reported under the applicable tax law, he acts illegally. The taxpayer is in such circumstances concerned whether he will be caught by tax authorities or even by the prosecuting authorities. Tax avoidance on the other hand, runs within the tax law frames and represents using loopholes to lower tax liability. Conversion of personal income to capital income, taxed under a lower tax rate, is such a typical example. The taxpayer in such cases, does not hide from the tax authority. To the contrary, he will even declare his transaction before them, so that he would achieve the desired goal. Sandmo wonders also how tax avoidance is any different from reacting to higher prices with buying less products than usually. If e.g. flight transport prices increase, and we use railway instead, do we avoid taxes? A very simplified explanation of tax avoidance would thus be that it represents actions causing an unintentional though legally compliant consequence of tax regulation. These are actions, incompliant to the purpose of regulation, however, compliant by the book (Sandmo, 2005, p. 645).

Strategies of MNE's are tax planning and using the loopholes and mismatches of tax rules for the purposes of artificial profit shifting to zero or minimal tax rate jurisdictions, where they do not perform any economic activity, or the latter is performed in a very limited scope. They are cutting their tax bases using tax recognised payments, e.g. interest and royalty payments. Most BEPS practices are legal, i.e. within the frame of tax avoidance. Nevertheless, such practices are unfair, since they undermine integrity of tax systems. Cross-border business models of MNEs are using BEPS to gain competitive advantage against enterprises doing business locally (Organisation for Economic Co-operation and Development (OECD), 2019).

<sup>1</sup> Court of justice of the European Union.

<sup>2</sup> See also McBarnet, 1992, p. 60.

## Anti-BEPS Measures of the OECD

As aforementioned, in October 2015 the OECD presented 15 reports on actions that should contribute to preventing or limiting harmful BEPS practices of MNEs. Actions of effected jurisdictions were especially motivated by the last financial crisis and various scandals, caused by several data leakage incidents on business of MNEs (e.g. LuxLeaks, Panama Leaks). Public became interested in subject theme and country leaders promised to take actions. The justifiable fear was that if no unified measure is taken soon, governments will seek unilateral measures to gain political points, which would have disrupted the established international tax system and cause even more loopholes, mismatches, i.e. BEPS opportunities as well as double taxation.

The purpose of international taxation regulation was always preventing double taxation and, though ineffectively, misuses of tax system. The fact that MNEs found opportunities to avoid tax outside of said purpose, should not serve for dismantling the international tax system as a whole. Namely the rules on preventing double taxation helped in globalization, which resulted also in economic growth and poverty limitation, not only in tax avoidance and evasion. The goal is thus to keep a stable and secure international tax system and at the same time adjust its institutes where their purpose was corrupted, and they were used for BEPS. The action plan is designed to close tax avoidance loopholes in the patchwork of domestic fiscal laws and bilateral tax treaties, and to correct the corrosive impact of tax competition (Van Apeldoorn, 2016, p. 478). Using the loopholes in corporate income taxation is undoubtedly declared and deemed as an unfair tax practice of the MNEs (Schreiber, 2015, p. 104). Justifiable means of preventing double taxation shall, however, remain a guideline and a goal in implementing anti-BEPS rules. The anti-BEPS actions are attacking misuse of tax benefits, where they are not intended and justified. In other words, MNEs performing a substantial activity in a certain jurisdiction should not be impacted or denied tax benefits that eliminate or limit double taxation<sup>3</sup>. To prevent negative impacts of anti-BEPS measures where tax benefits are justifiable and compliant to their true purpose, economic reality will be regarded instead of paper reality, aiming to divide harmful practices from good, not tax only motivated ones.

In light of the abovementioned, the OECD's anti-BEPS reports recommend or bind the countries to take necessary actions by either implementing new tax rules into their

legislation or amend the existing ones. These reports are comprehensive and by hundreds of pages per report also impossible to be summarised shortly. Hence, we state herein the measures and only very shortly explain their main focus and aim. For detailed reading, readers are directed to OECD's webpage, where all reports and other useful anti-BEPS material are available for free of charge access.

### 1) Action 1: Tax challenges arising from digitalisation

Action 1 deals with challenges that new digital businesses and transactions bring to the traditional tax systems. Considering high reliance on intangibles, internet and technology, digital companies are assumed to be particularly apt at optimising their corporate structures by navigating between national tax regimes in order to lower tax bases in places of factual value creation. To some extent, this is even characterised as unfair competition between traditional industries and companies that have embraced new technology (Lee-Makiyama & Verschelde, 2016, p. 56). Where business is run online and globally, the aim of anti-BEPS action plan is to find effective measures to follow and detect the place of profit and to tax it in the place, where it creates value. The digital world makes this task even more difficult because it facilitates cross-border collaboration, production, and sales of intangible goods and services. Factors, such as the use of new payment systems, e.g. bitcoin and the enhanced trading of personal information for "free" services in the cross-border business-to-consumer context. Accordingly, hybrid entities, which take advantage of different national laws that promote dissimilar and often conflicting tax outcomes, may be deployed to a greater extent to take advantage of this new global reality. Similarly, enhanced global activity in the digital world leads to more treaty shopping to take advantage of treaties with countries that have low- or no-income taxes (Cockfield, 2014, p. 937).

Action 1 basically considers other anti-BEPS actions, whereby they shall be adequately adjusted to digital economy. When an enterprise maintains a significant digital presence in an economy, it may still lack a *nexus* to it, resulting in the fact that it is not taxable in it under the existing international tax rules. The focus of Action 1 is put on how taxing rights on income generated from cross-border activities should be allocated among countries, and the suggestion that the changes caused or facilitated by digitalisation – notably scale without mass, heavy reliance on intangible assets, and the importance of data – require to revisit some fundamental aspects of the international tax system (so-called 'profit allocation' and 'nexus' rules) (OECD, 2019a).

<sup>3</sup> See also (Pinkernell, 2013, p. 739).

## **2) Action 2: Neutralising the effects of hybrid mismatch arrangements**

Interaction of various jurisdictions in combination with application of international tax rules, means also different and incoherent interpretation of certain institutes, causing different tax treatment of the same institute among various jurisdictions. OECD BEPS Project tackles the misuse of hybrid instruments and hybrid financial instruments that create tax optimization opportunities for MNEs, since hybrid mismatches can result in the fact that less or no tax is paid in the end (Rust, 2015, p. 89). E.g. an entity resident in State A provides a convertible loan to an entity resident in State B. State B treats payments arising out of such a loan to be deductible interest, whereas State A considers such payments to be dividends and allows a participation exemption. The taxpayer enjoys tax favourable treatment in both jurisdictions due to the difference in qualification of the payment (Govind & Zolles, 2018, p. 235).

Slovenia adopted hybrid mismatches rules in October 2019, within the process of adopting the EU ATAD<sup>4</sup>.

## **3) Action 3: Controlled Foreign Company (hereinafter: CFC)**

One of the most typical means of profit shifting is allocation of the profit to subsidiaries in low or zero tax jurisdictions. MNEs were establishing subsidiaries in such jurisdictions, however, such establishment may also be well founded when it has economic sense and purpose. Where such subsidiaries are established for actually doing business in a certain jurisdiction, providing that a subsidiary in fact has a certain degree of substance (e.g. staff, assets, significant functions), the issue of subsidiaries, even in low tax jurisdictions, is not problematic. Where, to the contrary, a subsidiary is established only or mainly for tax purposes, without justifiable business or financial reasons, the Action 3 provides that countries shall implement such rules that the income, shifted to such controlled entities, will be able to be re-allocated back to the parent company and taxed according to tax rules, applicable in their tax jurisdiction.

Slovenia implemented CFC Rules with January 1<sup>st</sup>, 2019. The CFC Rules were implemented under the ATAD of the EU.

## **4) Action 4: Limitation on interest deductions**

Interest payments are generally tax deductible. MNEs found the way to lower their tax bases by financing their subsidiaries by debt instead of equity. Enterprises of high tax jurisdictions were paying interests to related persons of lower tax jurisdictions, causing tax base erosion in high tax jurisdictions and profit shift to low tax jurisdiction. A well-established rule in the field is thin capitalisation, providing that debt financing should not exceed a certain relation to equity financing. Moreover, the interest payments shall always be determined and paid according to the Arm's Length Principle. It is now being recommended to adopt further interest deduction limitation rules based on fixed ratio rules, limiting tax recognised interest expenses and economically equivalent payments in comparison to EBITDA level (net interest/EBITA ratio; OECD, 2016).

Slovenia currently regulates thin capitalisation rules, whereby interest on the loans, granted by the qualified 25% direct or indirect shareholder, when such loans exceed four times the amount of the share of the relevant shareholder in the taxpayer's equity (loan surplus), determined with respect to the amount and the period of the loan surplus within the tax period, are non-deductible, unless the taxpayer proves that such a surplus could be achieved also towards non-related creditors. With respect to loans that do not represent the loan surplus, the interest on such loans, received from related persons, may be considered deductible only up to the amount of the last published recognised interest rate, which was known at the time of granting the loan, unless the taxpayer proves that he would under the same or comparable circumstances receive the loan under an interest rate, which is higher to the recognised interest rate also from a non-related creditor. Interest limitation rules are also regulated in Art. 4 of the ATAD. However, the European Commission determined Slovenian thin capitalisation rules as adequate and granted an exception, under which Slovenia may postpone implementation of interest limitation rules amendments to year 2024.

## **5) Action 5: Harmful tax practices**

Action 5 represents the minimum standard to be implemented by the countries. It addresses preferential tax regimes, mostly the issues with their detection and monitoring. Action 5 elaborates further on the nexus approach, stressing the evaluation of substantial activity in case of intangible assets. A simultaneous automatic exchange of tax decisions (e.g. advanced pricing agreements, other unilateral transfer pricing agreements, agreements of permanent establishments, actions of related entities, etc.) that represent a BEPS risk was also agreed. The latter is

<sup>4</sup> Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market OJ L 193, 19<sup>th</sup> July 2016, p. 1–14.



of particular importance, since the lack of transparency of specific tax regimes is one of the reasons why they are harmful and trigger BEPS opportunities in the first place.

#### **6) Action 6: Prevention of tax treaty abuse**

One of the biggest success of the international taxation system is the network of bilateral international agreements, entered by the countries mainly to agree on the taxing rights with the purpose of avoiding double taxation (hereinafter “DTC”). Double taxation represented an obstacle to MNEs in expanding their business cross border, however it unintentionally provided options for misuse in form of e.g. treaty shopping. By using the latter, MNEs were achieving tax benefits that were not intended for their cases. Action 6 proposes amendments to the OECD Model Convention<sup>5</sup>, expressly eliminating the purpose of tax avoidance and evasion from the general purpose of the DTCs. A minimal standard to fight treaty shopping shall be implemented, together with the limitation on benefits rule and a principle purpose test. Action 6 is a minimum standard.

#### **7) Action 7: Permanent establishment status**

Permanent establishments (hereinafter “PE”) are often used to avoid taxes. Namely, its former definition in the most of DTCs enabled MNEs to avoid triggering PEs and consequently paying adequate taxes in countries where they had performed their activities. The main issue of the former definition were the exemptions, under which a certain economic presence was not deemed a PE, therefore not taxable in that economy. Such exemptions were e.g. ancillary activities (e.g. warehouse, marketing, exhibitions) and short-term projects in construction businesses. MNEs changed their usual distribution models to agencies, formally transferring all essential distribution functions to other related companies. In a country, where an enterprise previously paid taxes on sales profits, it now pays taxes only to agency commission profits. Agency commission incomes are often further reduced by payments for various management and maintenance services (e.g. management fees, IT fees, insurance fees). Action 7 stresses that where such function transfers are artificial, the PE status can no longer be avoided. Moreover, it establishes that where such functions are important and form a coherent activity with activities of other related entities, they cannot be deemed ancillary.

One of the most famous cases on the field of PE misuse is Amazon’s. Amazon is an international on-line retailer,

basing its business model on warehousing and fast delivery to customers. In countries, where Amazon held a warehouse, it has been avoiding triggering a PE due to warehousing being deemed ancillary activity under the DTC and usually also local tax regulations. Now, therefore, under Action 7 an activity cannot be deemed ancillary, when it forms a coherent activity with the other functions. It was recognised that warehousing is one of the main activities of Amazon, thus, cannot be deemed ancillary.

The short-term project exception was exploited enormously by the construction MNEs, which misused the exception by fragmenting the activities among related and unrelated parties and concluding several short-term contracts for the same project. Action 7 recommends implementing the anti-fragmentation rule to prevent such practices.

#### **8) Action 8 – 10: Transfer pricing**

The main goal of Actions 8-10 is connection of profits to the MNE’s created values. A special attention is given to hard-to-value intangible assets. An MNE member shall be entitled only to profit, attributable to its factual activity. Cash box companies are in the centre of attention.

#### **9) Action 11: BEPS data analysis**

The action envisages methodologies for data collecting and monitoring, measuring fiscal effects of harmful tax practices and impact of the BEPS actions. In 2015 the OECD determined that the cost of tax avoidance of MNEs amounted from 100 to 240 billion of dollars, which corresponds to 4-10% of the worldwide corporate income tax (OECD, 2019a).

#### **10) Action 12: Mandatory Disclosure Rules**

Action 12 recommends rules that will oblige taxpayers and their advisors to disclose aggressive tax planning arrangements. Tax authorities will be able to detect harmful tax practices in advance and they will be able to target such practices more effectively.

The most related to Action 12 is the EU DAC<sup>6</sup> 6 Directive, which was implemented also in Slovenia in June 2019.

<sup>5</sup> OECD Model Tax Convention on Income and on Capital.

<sup>6</sup> Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation and repealing Directive 77/799/EEC, OJ L 64, 11<sup>th</sup> March 2011, p. 1–12.

### **11) Action 13: Transfer pricing and Country-by-Country reporting**

The centre of Action 13 is the transfer pricing documentation, which shall be formed in 3 pillars: i) a master file, which can be prepared on a group level; ii) a local file, which is prepared for a local entity; and iii) Country-by-Country report. Moreover, under Action 13 all large MNE groups are liable to report by country aggregated data about their global income distribution, taxes paid and economic activity among the tax jurisdictions (hereinafter "CbC Reporting"). The purpose of CbC Reporting is to provide tax authorities first and at least minimum indications of economic activity of an MNE group on their territories, which can enable more targeted audits. Action 13 is a minimum standard.

Slovenia adopted the CbC Reporting and exchange rules within the DAC 4 implementation. The three-pillar transfer pricing documentation as also envisaged by Action 13 is thus already implemented.

### **12) Action 14: Effective tax dispute resolution**

Action 14 is the minimum standard as well and it aims to improve tax dispute resolution among the countries. The Mutual Agreement Procedure is well established tax dispute resolution tool, however, it proved to be time consuming and ineffective. Action 14 provides recommendations for improvements. The institute is important as a tool of adequate DTC interpretation.

Slovenia amended its rules on the Mutual Agreement Procedure in June 2019.

### **13) Action 15: Multilateral instrument (the "MLI")**

With Action 15, OECD aimed to simplify the implementation of necessary amendments into existing DTCs, by proposing a multilateral instrument. By concluding and ratifying the MLI, existing loopholes in DTCs are intended to be eliminated, while the countries are able to avoid new and often hard bilateral negotiations in amending all of the DTCs. Nevertheless, MLI provides a lot of options available for countries' discretion, which makes the use of the MLI as well as the DTCs relatively complicated. Some countries, Slovenia as well, are preparing consolidated texts of the DTCs, simplifying the use of newly amended DTCs. The release of the MLI constitutes an important step towards the most significant re-write of international tax rules in a century. It is the multilateral convention enabling the simultaneous amendment of more than 3,000 existing bilateral conventions for the avoidance of double

taxation. It aims at eliminating loopholes and mismatches among them, which are susceptible to allow aggressive tax planning. In 39 articles, it implements Actions 2, 6, 7 and 14 of the BEPS Project, regarding hybrid mismatches, treaty abuse, artificial avoidance of permanent establishment status and dispute resolution of international tax disputes (Valente, 2017, p. 219).

Slovenia was among the first 5 countries to ratify the MLI, which is valid on its territory as of July 1<sup>st</sup>, 2018.

## **Impact of Anti-BEPS Measures on Business of MNEs**

After presenting very shortly the main issues dealt with the OECD 15 anti-BEPS actions, we evaluate in the remainder of the article, which actions and to what extent they impact business performance of MNEs, providing that the countries of their business will in fact implement and more importantly execute efficiently, not only the minimum standards but also other recommended actions. We note that international business might be impacted in practically every aspect. From market expansion to inter-company transactions, doing business among related parties will have to adopt to new tax law developments. Nevertheless, we have selected some of the most obvious impacts, i.e. we assess, how will the established international business models, consulting and digital businesses, mergers and acquisition (hereinafter "M & A") practices, have to adapt to be tax compliant.

### **A) Business Models**

One of the main conclusions, which can be derived from all of the adopted anti-BEPS actions, is that business models that serve the purpose of decreasing or even avoiding/evading tax liability are endangered. Enterprises which survive only due to the tax purposes, especially cash box or shell companies and conduit companies, will most probably become inefficient within the MNE group and the MNEs will gradually withdraw their business in countries, where their economic presence is intended for tax or mainly for tax purposes. Severe consequences to profits of enterprises, forming an MNE group, are not expected in countries, where enterprises execute significant value creating functions, since tax benefits are being reserved for active conduct of business (i.e. the "ABC Rule") only (Klink, 2016, p. 7).

It follows that where economic or other substantial presence of an MNE is established for purposes of e.g. obtaining DTC tax benefits, Action 6 shall prevent such misuse of

the DTC, combined with Action 15. If a tax authority will determine that a transaction was performed mainly for tax purposes, it shall deny the otherwise applicable tax benefit. Tax authority shall use the limitation of benefits rule and the principle purpose test subsequently to determine if the main or one of the main purposes of a transaction is decreasing or avoiding tax.

Furthermore, the CFC Rules under Action 3 will cause income re-allocation in the events of related entities without significant substance, back to its parent company, where they will be taxed under the tax law of the parent company. In this respect, the positive effects of the existing hybrid mismatches shall also be taken into consideration in doing cross-border transactions. Loopholes and discrepancies in tax treatments of hybrid instruments should now on be settled and not available for exploitation any longer. However, different approaches and non-mandatory nature of the majority of anti-BEPS actions may fail to close the loopholes or even create new ones.

The other aspect that is on the spotlight of the BEPS project is debt financing among the group. As already explained briefly above, Action 4 of the OECD anti-BEPS project tackles BEPS aimed to lower the tax base by tax recognised interest payments, which may be excessive or even contrary to the arm's length principle. The MNEs will have to balance debt financing and review existing financing models.

One of the main points of the entire OECD anti-BEPS project is finding the economic reality instead of relying to the paper reality. Tax authorities shall look behind the contractual provisions, especially when auditing payments related to intangible assets. Intangibles are by their nature mobile and represent one of the most important and commonly used tools in BEPS practices. Tax authorities will seek the nexus among the executed payments and value created. Functions transferred on paper will be revised according to the factual background of the functions *de facto* performed. With the intangibles the "DEMPE" function analysis will be emphasised, meaning that to avoid income re-allocation for tax purposes, the MNEs should review where they have allocated development, enhancement, maintenance, protection and extortion of the intangibles functions and if such allocation matches the factual place of the function performance or not.

Enhanced transparency (Actions 5, 12, 13), especially automatic and simultaneous exchange of data and tax decisions, should in theory enable the tax authorities targeted and effective audits of MNEs' international operations. Important indicative data are being reported throughout all the markets of an MNE group's business performance. It will be difficult for MNEs to hide conduit or other

non-function enterprises in their ownership chains from the tax authorities. Consequently, tax advisors and internal tax staff will obtain a more significant role in ensuring tax compliance. Tax departments within the group will have to cooperate in assisting and providing the relevant data to all the members within the MNE group to ensure consistency and coherent reporting. Administration and tax advisory costs will therefore increase.

Transfer pricing schemes of MNEs are being revised as well. The existing transfer pricing documentation will necessarily have to be revised in order to verify, if it still includes sufficient data and analyses, as recommended by anti-BEPS Actions 8-10, 12 and 13. This will definitely increase costs of preparing compliant transfer pricing documentation, which are already very high, especially for local companies of smaller markets.

Mobility of the staff is particularly common with MNEs. E.g. postage of leadership staff to manage a related company, sending employees for education, posting employees to work on a specific project abroad, allowing home offices abroad, are being done within daily business. MNEs will have to revise such practices and assess their tax liabilities in foreign markets anew. Namely, if certain functions travel with staff to other countries, a PE may be triggered, under recommendations of anti-BEPS Action 7, even more often and faster than up to date. Nevertheless, practice shows that MNEs as employers are often unaware of travels of important staff and its tax implications. Hence, MNEs will have to establish a system of controlling, to monitor the place and functions of their hired staff.

## B) Impact to Consulting Business

The public recognised tax, legal and financial consultants as the associates to MNEs in conducting harmful BEPS practices. Selling innovative and effective tax planning arrangements was practically one of the main income sources for the most successful international tax advisory companies. Action 12 intends to limit such cooperation by imposing reporting liabilities on potentially harmful tax schemes to tax authorities by the consultants themselves. Tax consultancy firms will have to implement measures to comply with new reporting demands and a decrease in income in respect to selling harmful practices is expected. However, such decrease may be replaced by tax compliance advisory services, which will probably become of a high demand considering the uncertainty and complexity of the new measures. Firms specialised in specific international taxation topics will gain advantage in comparison to general tax advisory firms. Services of such specialised experts will become more expensive in consequence.



### C) Digital Business

MNEs of digital economy represent a special challenge for legislators. Namely, it is difficult to establish the place of their economic presence, of their nexus. Action 1 is one of the broadest and least clear actions, leaving room for country specifics, causing insecurity regarding future liabilities for digital MNEs. Recommendations on the field of digital economy are not very specific, causing a major legal insecurity and unpredictability of tax impacts. This causes issues for digital companies with respect to entering new markets, pricing of their products and business strategy (Flynn & Bates, 2016, p. 15). Amended PE definition within the Action 7 represents a high risk of triggering unknown PEs for digital companies, causing difficulties in assessing tax liabilities. Digital companies often use mobile employees, namely they enable employees home offices in various countries. When such employees will perform functions, essential for the business (e.g. software development), a PE may be unintendedly triggered in the place of employee's residence. Unintended PEs represent risk in potential penalties for omission of tax reporting and payment as well as additional tax payment and administrative burden in the event of recognised PEs. A place of a hired server may in some cases of digital companies (e.g. companies whose main purpose is offering data storage or hosting) represent a PE risk. A thorough review of the entire business model, existence of mobile employees as well as location of crucial assets, will have to be performed in order to detect unintended PEs and to manage associated risks. Increased reporting liabilities within Action 12, 13 and 5, may unintentionally provide grounds for tax audits, hence digital MNEs shall be well aware of the data, being reporter to tax authorities throughout the entire group.

### D) M & A Transactions

Anti-BEPS actions will impact all phases of a M & A transaction (targeting, due diligence, structuring and evaluation). In the post-transaction phase also, the integration and compliance of reporting will be impacted. Limitations within the scope of Action 2 and 4 will impact financing of the transactions, especially debt financing models. Professional investment funds, e.g. private capital funds and pension funds will be impacted by Actions 6 and 7 regarding the access of DTC tax benefits, economic substance requirements and amended PE definitions. Limitations of preferential tax regimes and innovation financing will cause previously tax favourable arrangements inconvenient. Anti-BEPS actions represent enhanced tax liability and tax compliance cost that could impact the risk, structure and value of a transaction. Value of a target will be harder to determine, whereby investors, willing to undertake tax risks and of the knowledge to

evaluate and recognise them, will have a big advantage on the M & A market. The tax due diligence will be oriented to the past and to the future, whereby tax advisors shall have the capacity to foresee the consequences of anti-BEPS actions implementation to the tax position of the entire MNE group. Tax policy of the target may undermine or crush the tax policy of the entire group. Action 12 will enable tax authorities to detect tax motivated transaction to tax authorities in the very early stage of the transaction (Eagers & Bennett, 2016, pp. 30–33).

Upon acquisition of a group, tax due diligence will have to be performed in various countries due to numerous specialties, available to the countries for implementation. Due to emphasised tax compliance, the price of tax due diligences is expected to increase. It is recommended that tax experts take part in contract drafting and negotiating. Potential tax risks shall be taken into account in the representations and warranties catalogue and indemnities for additional tax liabilities should be agreed for detected risks. A special attention should be granted to proper function and risk allocation and usage of proper transfer pricing methods. Compliance with reporting liabilities should also be thoroughly reviewed. Additional warranties should be agreed on the field of PEs, namely the seller should warrant that to the best of his knowledge, he is not aware of any cross-border activity that could form a PE or vice versa, that he is aware of all cross-border activity and that to the best of his knowledge, such activities do not trigger PEs on relevant markets.

A general tax warranty clause, which was usually agreed in purchase agreements in the past, may also cover all mentioned tax risks. However, the sellers are strongly advised to avoid too broad tax warranty or indemnity clauses. The anti-BEPS actions can be so far reaching that sellers, who are not reassured of their international tax position, should refrain from agreeing to general tax warranty or indemnity clauses in agreements. If they would nevertheless accept to agree to general tax clauses, attention to proper liability limitation should be given. It is thus preferable for both contracting parties to precise tax clauses in the agreements as strictly as possible or to understand the consequences of agreeing to broad clauses and take the unknown additional liabilities into account when setting a price.

### Conclusion

MNEs had innovatively and effectively used the loopholes in international tax system, which were caused due to the collision of various national tax systems on the otherwise global market. Tax legislation sovereignty is a difficult international law topic and so far, the countries were protecting

their tax systems from harmonisations. Access to secret information, several information leakages, combined with financial crisis, are only a few facts that attracted public attention to unfairness of taxation of MNEs in comparison to local companies. It has become politically favourable to claim to protect tax bases in countries of MNEs' economic presence. International institutions had to act in their attempt to prevent unilateral measures that would definitely follow, if no effective unified solutions would be offered to legislators. The OECD BEPS project is thus a good attempt to protect tax bases where they are supposed to be taxed and prevent double taxation, which would be caused by unilateral measures of the countries. Maintaining effective tools to prevent and eliminate double taxation are hence of crucial importance to MNEs and global economy.

Nevertheless, we cannot totally avoid the unfairness of the public opinion and focus of legislator to harmful tax practices of the MNEs. In our opinion local companies should not be disregarded when assessing the reasons of low corporate income tax yields. It is a fact that interactions of various tax systems on the global market provide more opportunities for loopholes and their misuse in doing international business. However, especially in small export-oriented countries, like Slovenia, legislators should implement further restrictions to international transactions with caution in order to prevent foreign investment leakages from their economies. Potential amount of avoided corporate income tax should always be weighed against other positive fiscal effects that incur as a consequence of employments, investment, innovation, sale, etc. MNEs bring know-how, technology and usually contribute to the growth of small economies<sup>7</sup>.

As we have indicated above, implementation of anti-BEPS actions will increase cost of doing business internationally. MNEs will be even more prudent and cautious when entering new markets, especially where they will encounter higher tax liabilities and administration in comparison to expected earnings. On the other hand, implementation of envisaged actions will represent economic burden to fiscal authorities as well. Undeveloped tax jurisdictions will find it difficult to implement or execute the anti-BEPS actions due to poor infrastructure and incompetent staff. Advanced tax jurisdictions, e.g. most of the OECD member states and member states of the EU, are already executing actions to prevent or limit anti-tax avoidance practices for years and they have an advantage over emerging tax jurisdictions. Moreover, Burgers and Mosquera argued that the participation on equal footing of developing countries in the BEPS

Project are not sufficient to legitimise the role of the OECD and the BEPS 44 group of countries that participated in the BEPS Project in setting international tax standards for developing countries. The reason is that there has not been a true decision-making process. Since the content of BEPS Actions has been decided by the BEPS 44 group with developing countries having only a consultative role (Burgers & Mosquera, 2017, p. 31). Nevertheless, positive effects of anti-BEPS measures could hardly be effectively measured so far, which is the ground for the OECD to recommend improvements of analytics and reporting (e.g. especially within Action 11 of the BEPS Project), which will enable the OECD to measure the scope and consequences of BEPS practices as well as the impact of anti-BEPS measures. It also has to be emphasised that the majority of the anti-BEPS actions leave discretion to the countries in choosing proper means of preventing certain BEPS practices, providing that there is a lot of room for creating further loopholes in international tax system which MNEs will be eager to use.

Discrepancies among national tax systems and potential unilateral measures of tax jurisdictions represent a risk for uninterrupted functioning of common markets, such as the internal market of the EU. With this respect the institutions of the EU aimed to prevent fragmentation of national tax policies and unilateral measures of its member states that could impair functioning of the internal market of the EU and adopted several anti-tax avoidance measures for the EU member states to implement them<sup>8</sup>. Since 22 of 28 EU Member States are also part of the OECD, it was necessary to provide for a common implementation of the BEPS Action Plan that could also fit with the EU legislation and the relevant CJEU case law. For this reason, the instrument of the Directive was the most appropriate in order to ensure a coordinated and uniform application of rules which substantially affect the single market (Ginevra, 2017, p. 137). In this light, the Anti-Tax Avoidance Directive (the ATAD<sup>9</sup> and ATAD II)<sup>10</sup>, requires member states to implement adequate legal measures to combat harmful tax practices. The ATAD provides a legal frame for adopting CFC Rules, Interest Limitation Rule and Hybrid Mismatch Rules, whereby it also provides measures, outside the OECD anti-BEPS project, i.e. General Anti Avoidance Rule and Exit Taxation Rule. Nevertheless, the EU anti-BEPS measures share the problem with the OECD BEPS Project, i.e. setting only

<sup>7</sup> E.g. Durst argued that the most important impediment to effective control of base erosion is the pressure of tax competition – namely, the fear that effectively imposing income taxes on inbound investors will deter employment and economic growth (Durst, 2014, p. 3).

<sup>8</sup> The EU Anti-Tax Avoidance Package (see <https://www.consiliium.europa.eu/en/policies/anti-tax-avoidance-package/>).

<sup>9</sup> Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market OJ L 193, 19<sup>th</sup> March 2016, p. 1–14.

<sup>10</sup> Council Directive (EU) 2017/952 of 29 May 2017 amending Directive (EU) 2016/1164 as regards hybrid mismatches with third countries OJ L 144, 7<sup>th</sup> June 2017, p. 1–11.

minimum standards or recommendations within the soft EU law to be implemented, leaving discretion to the EU member states to take stricter actions, which may fail the cause on the subject field – i.e. to prevent unilateral actions of the member states, securing functioning of the internal EU market. Discretion and unclarity regarding execution of

anti-BEPS actions mean uncertainty, which contradicts to one of the founding principles of the tax law, i.e. certainty in tax matters. Taxpayers must be aware of tax implications of their businesses in advance. Only by taking the applicable taxes into account, they will be able to properly evaluate their transactions.

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# Anti-BEPS ukrepi in njihov učinek na uspešnost multinacionalnih podjetij

## Izvleček

Prispevek predstavlja škodljive davčne prakse mednarodnih podjetij (MNP) in boj mednarodnih organizacij proti njim. V prispevku se osredotočamo na projekt Organizacije za gospodarsko sodelovanje in razvoj (OECD) za preprečevanje erozije davčne osnove in prenašanja dobičkov (projekt za preprečevanje BEPS), in sicer na 15 ukrepov, sprejetih v okviru tega projekta, ki jih predstavljamo v prvem delu prispevka z uporabo deskriptivne in analitične metode. V drugem delu s pomočjo sintetične in kritične metode analiziramo vpliv omenjenih ukrepov na izbrana področja mednarodnega poslovanja. Naši zaključki kažejo na to, da se bodo MNP-ji morali prilagoditi novim davčnim regulativam, kar bo povzročilo tudi znižanje ravni njihovih dobičkov, saj za zniževanje davčnih osnov ne bodo imeli več na voljo uveljavljenih škodljivih davčnih struktur. Hkrati pa smo zaključili, da obstoječi pravni pristop pri uvajanju novih ukrepov vodi v pravno negotovost v davčnih zadevah. Zaradi obsega analizirane problematike je bilo nemogoče poglobljeno obravnavati posamezne ukrepe, zato bralcem na splošno predstavljamo značilnosti in cilje predmetnih ukrepov, ki so pomembni za razumevanje naše ocene njihovega vpliva na izpostavljena področja mednarodnega poslovanja. Prispevek bo uporaben v literaturi in praksi, saj omogoča splošen pregled trenutnih in pomembnih premikov v mednarodnem davčnem pravu, ki jih bodo MNP-ji morali upoštevati pri čezmejnem poslovanju.

**Ključne besede:** BEPS, OECD, mednarodno davčno pravo, davki, KIDO, davčno načrtovanje, prenos dobičkov, erozija davčne osnove, davek od dohodkov pravnih oseb