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**TO ALL MEMBERS**

**TECHNICAL**

## Direct Taxation

## BEPS: Changes in international tax

At the recent luncheon hosted by CTIM in Kuala Lumpur on 19 May 2014, YBhg Tan Sri Mohd Shukor bin Hj. Mahfar, CEO of IRBM, spoke briefly on base erosion and profit shifting (BEPS). YBhg Tan Sri mentioned that the IRBM is working on a BEPS action plan which could be tabled as early as September 2014. The focus of the BEPS action plan would depend on the Organisation for Economic Co-operation and Development's (OECD) BEPS initiatives.

### What is BEPS?

BEPS refers to tax planning strategies which exploit gaps or mismatches in tax rules of different tax jurisdictions (e.g. home and host countries' tax jurisdictions) in order to make "profits" disappear for tax purposes or to shift profits to tax jurisdictions where the taxes are low resulting in little or no corporate taxes.

BEPS can be detrimental as follows:-

- It can distort business competition by giving businesses that operate cross-border a competitive advantage over businesses that operate domestically;
- It may lead to inefficient allocation of resources by distorting business investment decisions towards activities; and
- It can undermine voluntary compliance by all taxpayers when multinational corporations are seen to be legally avoiding income tax.

The OECD does not see BEPS as a problem created by businesses. Apart from some cases of abuse, the issue lies with the tax rules. As businesses cannot be faulted for using the rules put in place by governments, it is therefore the governments' responsibility to revise the rules or introduce new rules.

### What is being done to address BEPS?

As BEPS strategies take advantage of gaps or mismatches between tax rules of different tax jurisdictions, there is a need for an internationally coordinated approach to facilitate and reinforce domestic actions to protect tax bases and provide comprehensive international solutions to respond to the issue. The BEPS Action Plan initiated by the OECD in 2013 provides a consensus-based plan to address these issues as part of on-going efforts to ensure that the global tax architecture is equitable and fair.

The OECD's BEPS Action Plan will result in fundamental changes to the international tax standards and are based on three core principles: coherence, substance and transparency. The BEPS Action Plan sets out the following actions:-

Actions to ensure coherence:-
- Neutralise the effects of hybrid mismatch arrangements;
- Strengthen controlled foreign companies (CFC) rules;
- Limit base erosion via interest deductions and other financial payments; and
- Counter harmful tax practices more effectively.

Actions to align taxation and substance:-
- Prevent treaty abuse;
- Prevent the artificial avoidance of permanent establishment (PE) status; and
- Assure that transfer pricing outcomes are in line with value creation.

Actions to ensure transparency, while improving certainty:-
- Establish methodologies to collect and analyse data on BEPS and the actions to address it;
- Require taxpayers to disclose their aggressive tax planning arrangements;
- Re-examine transfer pricing documentation; and
- Make dispute resolution mechanisms more effective.

For more information and updates on the OECD's BEPS initiatives, please visit the OECD's website at http://www.oecd.org/tax/beps.htm.