BEPS' Bait & Switch: OECD Pillar II GloBE Comments and Recommendations

Kluwer International Tax Blog
December 5, 2019

William Byrnes (Texas A&M University Law)

Please refer to this post as: William Byrnes, 'BEPS' Bait & Switch: OECD Pillar II GloBE Comments and Recommendations', Kluwer International Tax Blog, December 5 2019, http://kluwertaxblog.com/2019/12/05/beps-bait-switch-oecd-pillar-ii-globe-comments-and-recommendations/

Our 14-page comments and recommendations of 14 tax professionals and academics from 11 countries raise additional issues and concerns, and propose additional recommendations to undertake a detailed cost benefit analysis of the existing BEPS Actions prior to taking such drastic measures. Our 14 pages of comments and an appendix are available here on SSRN.
We applaud the OECD's tremendous effort since 2013 to work globally via the Inclusive Framework to address Base Erosion and Profit Shifting. GloBE conflicts with and harms the OECD's goals of BEPS, and like Pillar I, is a distraction of resources and unlikely to obtain broad consensus. The OECD 2013 Action Plan Report on BEPS states as follows:

> *No or low taxation is not per se a cause of concern, but it becomes so when it is associated with practices that artificially segregate taxable income from the activities that generate it. In other words, what creates tax policy concerns is that, due to gaps in the interaction of different tax systems, and in some cases because of the application of bilateral tax treaties, income from cross-border activities may go untaxed anywhere, or be only unduly lowly taxed.*

From this statement it can be clearly inferred that from the origination of the BEPS project, supported by the Inclusive Framework, the issue was not about 'no or low taxation of the income' but rather BEPS has been concerned to address cases of double non-taxation or no or low taxation associated with practices that artificially segregate taxable income from the activities that generate it. Therefore, defining the scope of Pillar 2 as a global anti-base erosion (GloBE) proposal which seeks to address remaining BEPS risk of profit shifting to entities subject to no or very low taxation appears misleading and it does not fit into the original definition and the original mandate of the BEPS project.

Pillar 2 is a deviation from the well-established tax principle – that was the genesis of BEPS – which is to tax income where value is created. It is too early to discuss, must less codify, a new BEPS 2.0 project while BEPS 1.0 is still not fully implemented in many countries and the economic outcome of the anti-abuse measures on the tax revenues collected by States that have already implemented BEPS 1.0 measures are still not determined much less analyzed.

We thus recommend that the OECD restate that the purpose of BEPS is about artificial segregation between profits and activities that originated those profits. Also, we recommend that a thorough impact assessment should be conducted by the OECD, ideally showing the additional impact compared to the already implemented BEPS actions before making any major changes to the existing international tax system. We believe that with the elimination of harmful tax regimes and the alignment of substance and profit, a major part of the previously assessed BEPS should be verified in the upcoming report on BEPS Action 11. The OECD should therefore have robust data at hand to provide the members of the Inclusive Framework that an informed discussion and decision based on understanding the cost-benefit impact of the implementation of any potentially complex aspects of the Pillar 2 framework.

Regimes meeting "BEPS Action 5" standards should be carved-out.

A main concern is that compliance with BEPS Action 5 does not automatically mean that a jurisdiction is not targeted under GloBE. On the contrary: most likely the majority if not all the preferential tax regimes that meet this BEPS minimum standard will fall under the application of Pillar 2. This would question the efforts made by jurisdictions to introduce BEPS compliant regimes, sometimes less than a year after they have been introduced. And ultimately may challenge the value of the minimum standards themselves.

Furthermore, it is worth recalling para. 24 of Action 5 final report when stated that: *Action 5 specifically requires substantial activity for any preferential regime.* Seen in the wider context of the work on BEPS, this requirement contributes to the second pillar of the BEPS Project, which is to align taxation with substance by ensuring that taxable profits can no longer be artificially shifted away from the countries where value is created. Again this demonstrates that regimes which are compliant with Action 5 minimum standard should be carved-out as they meet BEPS concerns and they meet the original premise of the 2013 BEPS project. Including these regimes under the GloBE represents a contradiction: if Pillar 2 aims at addressing other BEPS risks but Action 5 already addresses BEPS risks related with preferential tax regimes it is hardly conceivable how such regimes cannot be automatically compliant under Pillar 2.

Attention is drawn to the EU law that allows a restriction of the four freedoms only if it is justified by overriding reasons of public interest such as the prevention of abuse.

Layering of Methods to Determine Tax Base Increases Complexity and Compliance Costs.

The OECD proposes that the starting point for the determination of the tax base will be the audited financial statements under the accounting standards of the headquarters jurisdiction prepared in accordance with the Generally Accepted Accounting Principles (GAAP) or the International Financial Reporting Standards (IFRS). The consolidation financial aggregate simply sums up legal entity financial reporting into a whole. In particular, intercompany transactions are eliminated in creating this aggregated accounting picture. This aggregation by itself gives no clues to functions performed, risks assumed and assets employed in relation to value creation.

The two standard approaches, GAAP or IFRS, have their differences and these will have to be reconciled to ensure accuracy and consistency in any analysis. Further, is the challenge posed by 'local' GAAP, as opposed to the Parent Country? Local countries are often required to present their required financial statements in terms of local GAAP. Local GAAP and Parent country GAAP often need reconciliation as accounts may be treated differently, posted above or below the operating profit line and thus influence the measurement of the tax base.

Financial Accounts are not 'fit for purpose' as tax accounts to determine tax base. Financial Accounts have a different objective, purpose, and audience than the Tax Accounts that have been built for a tax system. Hence, we think that there are significant challenges in the use of GAAP financial accounts to calculate and reconcile the tax base. The experience of the European Commission to abandon the GAAP financial accounts and develop a common consolidated tax base for the "CCCTB" does well illustrate the substantial difficulties linked to the endeavor of using a common standard to calculate the tax base. A CCCTB type common consolidated tax base could significantly increase the complexity and cost of compliance of adding another layer of required tax accounting data collection, remediation, and manipulation to determine the GloBE tax base.

In light of the Pillar I proposal to add its own additional unique layer of tax accounting to determine residual, we recommend that a thorough impact assessment should be conducted by the OECD to estimate the impact of compliance on both businesses and tax authorities of adding these layers to the current tax accounting systems required for national tax base determination.

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