Base erosion and profit shifting (“BEPS”) – Are you BEPS proof?

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BEPS is a term used by the Organisation for Economic Co-operation and Development (“OECD”) to describe tax planning strategies exploiting gaps and mismatches in tax rules so that profits disappear for tax purposes or profits are shifted to locations with little or no real activity and where profits are subject to little or no taxes.

Although BEPS is not illegal it distorts competition between those companies operating cross border and those operating domestically and it leads to inefficient allocation of resources and it seems unfair that some companies can legally avoid paying tax.

The OECD’s BEPS Action Plan is designed to redefine and revolutionise the taxation of companies across the globe. It is the first co-ordinated attempt to reach common objectives – in developed and developing economies – that we have seen in some time. Undoubtedly, the BEPS Action Plan is a major evolution in the international tax and transfer pricing landscapes and will have a lasting impact on multinationals globally.

The main objections of the Action Plan are to:

- develop a new set of standards designed to avoid double non-taxation;
- aligning taxing rights with substance; and
- improve transparency.

The issue actually lies with the tax rules themselves and

businesses cannot be faulted for using the tax rules put into place by governments to their benefit. Governments are therefore responsible to revise these rules or introduce new rules.

BEPS will have a substantial impact on multinational companies and the challenge for companies is to stay current with respect to changes in the various tax jurisdictions in which they operate.

Many multinational companies, especially the fast-growing ones, have not evaluated the potential impact of the Action Plan on its business operations.

Whilst we are in the midst of the OECD's BEPS project, it remains to be seen what the immediate impact will be on the transfer pricing space. The existing transfer pricing foundations are, broadly speaking, consistently applied worldwide – many jurisdictions have already enforced tough legislations in this respect. The BEPS considerations on intangibles, for example, are aligned with existing OECD guidelines, with the exception of the rules relating to the valuation of intangibles.

The immediate obligation for taxpayers will most possibly be the country-by-country reporting which instructs multinationals to disclose a full view of their global tax positions to authorities. From an operational point of view companies need to understand how to deal with the request from SARS to disclose its global value chain as part of the country-by-country analysis.

The new transfer pricing documentation standards adopts a 3 tier approach requiring multinationals to prepare a master file, a local country file as well as the country-by-country reporting. How will multinationals deal with the mandatory requirement for both a master file and local country file at the time of submitting the annual corporate income tax return.

There is a real risk that these new transfer pricing documentation requirements will overwhelm the compliance burden of taxpayers while the level of transparency could create multiple disputes.

The Action Plan also increases the importance of having a transfer pricing policy that is in line with the value creation within a group.

Essentially, BEPS has already impacted multinationals. With public discussions focusing on tax driven structures, authorities are permitted to threaten taxpayers with aggressive consequences.

The impact of BEPS is inescapable. With the OECD's timeline for implementation closing in December 2015, multinationals have a limited window of opportunity to act to ensure risks are identified and managed. Each multinational company, therefore, needs to assess its position with respect to the OECD BEPS guidelines so to address major concerns, to detect and understand the risks and to provide practical answers to the crucial problems. It is important to understand the implications and seek to address any risk that could have a dramatic impact.

Any assessment should not only focus on the direct tax implication, but it should also focus on any reputational risk that could arise from particular tax strategies followed. Boards of directors will have to decide what reputational risks they are willing to take to limit tax payments. However, these boards will also need to be advised on what to do to minimise these risks, even if it requires the unwinding of any aggressive tax strategies followed. The longer term priorities should include a review of all tax structures and the evaluation of the risks posed by such structures.

It is time to ask: "What do we need to do to become BEPS proof in the territories in which we operate?" and find out whether

the groups transfer pricing policy is indeed “BEPS proof”. Larger multinationals should already be engaging and gearing up for the changes ahead.