



# THE GOVERNANCE BRIEF

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## Adopting the New International Tax Rules and Standards

### How Developing Countries in Asia and the Pacific Stand to Benefit—If They Engage!

By Richard Highfield<sup>1</sup>

#### Introduction

Mobilizing the domestic resources of developing countries and making better use of international assistance has been the subject of considerable discussion over the past 2 years, and is a key direction and commitment reflected in the Addis Tax Initiative Declaration of 2015,<sup>2</sup> and the UN's Sustainable Development Goal 17 (Target 1):

*“Strengthen domestic resource mobilization, including through international support to developing countries, to improve domestic capacity for tax and other revenue collection.”*

This brief presents a major challenge for all developing countries, particularly their respective ministries of finance and national tax administrations that together play a critical role in setting revenue mobilization objectives, and determining strategies and approaches for their realization.

In a session at the International Monetary Fund (IMF)–World Bank Spring Meetings held in April 2016 titled “Collect More and Spend Better,” it was observed that billions of dollars of potential tax revenue remain uncollected each year in many developing countries, either due to poor tax system design or weaknesses in tax administration.<sup>3</sup> A fair

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<sup>2</sup> The Addis Tax Initiative (ATI) is a multistakeholder partnership to catalyze significant increases in efforts to improve domestic revenue mobilization so that partner countries can more effectively raise their own funds to invest in public services and other development needs. The initiative aims to address the billions of dollars lost every year due to narrow tax bases, weak administrative capacity, and poor tax compliance. For more information see <https://www.taxcompact.net/documents/Addis-Tax-Initiative-Briefing-Note.pdf>

<sup>3</sup> Seminar titled “Collect More and Spend Better: The Role of Capacity Development” held with the IMF's 2016 Spring Meeting. See [https://www.imf.org/external/POS\\_Meetings/SeminarDetails.aspx?SeminarId=119](https://www.imf.org/external/POS_Meetings/SeminarDetails.aspx?SeminarId=119)

**“Over the last 7 years, the OECD, together with many advanced and developing countries and regional tax bodies, have been working... to develop new rules and processes to strengthen the international tax system.”**

amount of this foregone tax revenue arise from practices that are facilitated by either:<sup>4</sup>

- (i) Lack of transparency of some countries’ banking and regulatory environments that enable tax evasion through offshore concealment of income and assets, as highlighted by the recent release of the so-called “*Panama Papers*;<sup>5</sup> and
- (ii) Weaknesses in the international tax system that enable profit shifting between countries and other tax irregularities, currently the subject of the OECD project on “base erosion and profit shifting” (known as BEPS) discussed in this brief.

Over the last 7 years, the OECD, together with many advanced and developing countries and regional tax bodies, have been working, with strong support from the G20, to develop new rules and processes to strengthen the international tax system.<sup>6</sup>

This governance brief outlines these developments, along with their rationale and expected benefits. In doing so, the brief seeks to encourage developing countries in Asia and the Pacific region to engage with the global processes now in place to oversee further development and implementation, where they have not already done so.

## Global Developments to Reform the International Tax System

International efforts to address weaknesses in the international tax system rely largely on two building blocks: (i) promoting transparency and exchange of information among jurisdictions for tax purposes; and (ii) tackling tax avoidance via the OECD/G20’s BEPS project. With considerable progress made to develop comprehensive proposals for reform in both areas, the focus of these international efforts has now shifted to their implementation on a global basis.

## 1. Promoting transparency and exchange of information for tax purposes

Taxation is a critical source of revenue for all governments, in particular for developing countries where revenue mobilization efforts produce far less tax revenue, relatively speaking, than in developed countries. The problem of tax evasion in developing countries is particularly acute, as tax evasion even by a wealthy few can have a relatively significant impact. In the absence of alternate revenue sources, the inevitable losers from tax evasion are those citizens who miss out on essential services they need to survive with minimum dignity and respect. The revenue needs of developing countries, in combination with the broader goals of nation building, highlight the urgency of increasing global transparency concerning the location of untaxed wealth that has been facilitated by bank secrecy and the inability of tax authorities to detect evasion.

### *Exchange of Information on Request*

The impetus for major changes to address the problems presented by the impervious practices of some jurisdictions, including bank secrecy, came in 2009 when, following the global economic crisis, G20 leaders declared that bank secrecy would no longer be tolerated and committed to take action against non-cooperative jurisdictions, including tax havens. In line with this commitment, many countries agreed to fight cross-border tax evasion together by committing to the international standard for exchange of tax information on request (EOIR) developed by the OECD, and by joining a restructured Global Forum on Transparency and Exchange of Information for Tax Purposes (Box 1). The work of the Global Forum, with 137 members as of end-December 2016, has enabled rapid implementation of the standard through extensive engagement with participating jurisdictions and a comprehensive peer review process.

### *Automatic Exchange of Information*

Further steps were taken to strengthen tax transparency in 2013 when G20 leaders committed

<sup>4</sup> ADB estimates that developing countries lost \$5.6 trillion in illicit tax flows over the period 2001–2010, which includes amounts lost through tax evasion; and Asia accounted for 61% of the total. ADB. 2012. *Anticorruption Policy: Enhancing the Role of the Asian Development Bank in Relation to Tax Integrity*. Manila.

<sup>5</sup> The “*Panama Papers*” refer to a collection of over 10 million documents created by Panamanian law firm (Mossack Fonseca) that detail financial and attorney–client information for over 200,000 offshore entities. The documents, which were leaked to a German newspaper, illustrate how wealthy individuals and public officials are able to keep personal financial information private. While offshore entities are often not illegal, reporters allegedly found that some of the law firms’ shell corporations were used for illegal purposes, including fraud, tax evasion, and evading international sanctions.

<sup>6</sup> The G20 (or G-20 or Group of Twenty) is an international forum for the governments and central bank governors from 20 major economies. It was founded in 1999 with the aim of studying, reviewing, and promoting high-level discussion of policy issues pertaining to the promotion of international financial stability.

**Box 1: The Global Forum on Transparency and Exchange of Information for Tax Purposes**

The Global Forum on Transparency and Exchange of Information for Tax Purposes is the multilateral framework within which work on transparency and exchange of information for tax purposes has been carried out by both Organisation for Economic Co-operation and Development (OECD) and non-OECD economies since 2000. Since its restructuring in 2009, the Global Forum has become the key international body working on the implementation of the international standards on tax transparency. The Global Forum ensures that these high standards of transparency and exchange of information for tax purposes are in place around the world through monitoring and peer review activities. In order to ensure worldwide participation in the benefits of increased tax transparency and international cooperation and to ensure that developing countries benefit from the new tax transparent environment, the Global Forum has a technical assistance program for its members.

There are two internationally agreed standards on exchange of information for tax purposes: (i) Exchange of Information on Request (EOIR); and (ii) Automatic Exchange of Information (AEOI).

The Global Forum currently has 137 members participating on an equal footing, together with 15 international organizations participating as observers. All member jurisdictions have committed to implementing the international standard on EOIR. The Global Forum conducts rigorous assessments of compliance with this standard, according to the elements set out in its terms of reference. In addition, more than 90 countries and jurisdictions have committed to implementing the new standard on AEOI. Work is currently underway to implement this standard, with the first exchanges occurring on a very ambitious timeline of 2017 and 2018.

Source: Global Forum on Transparency and Exchange of Information for Tax Purposes. <http://www.oecd.org/tax/transparency> (accessed 10 January 2017).

**“The Global Forum on Transparency and Exchange of Information for Tax Purposes is the multilateral framework within which work on transparency and exchange of information for tax purposes has been carried out... since 2000.”**

to the OECD proposal for Automatic Exchange of Information (AEOI) to be the new international standard, and fully supported further work by the OECD and G20 countries to present a single global standard in 2014. This work culminated in the development of the Common Reporting Standard (CRS) for automatic exchange of tax information. The CRS, which deals with the automatic exchange of financial account information, draws on the United States’ Foreign Account Tax Compliance Act (FATCA) initiative.<sup>7</sup> However, unlike FATCA, it is designed to meet the requirements of multiple jurisdictions and minimize the compliance burden

on financial institutions that must report to multiple jurisdictions.

Box 2 summarizes the key steps involved in implementing the new AEOI standard at the level of individual jurisdictions. Further information on the new AEOI standard can be found on the Global Forum’s website (<http://www.oecd.org/tax/transparency/>) and, in particular, in the guidance entitled *Automatic Exchange of Information: A Roadmap for Developing Country Participation, Final Report to the G20 Development Working Groups*.<sup>8</sup>

<sup>7</sup> FATCA is an initiative of the Government of the United States to combat tax evasion. Enacted in 2010, the FATCA legislation requires certain US taxpayers holding financial assets outside the United States to report those assets to the Internal Revenue Service (IRS). In addition, foreign financial institutions must report directly to the IRS information about financial accounts held by US taxpayers or by foreign entities in which US taxpayers hold a substantial ownership interest. Such reporting is intended to encourage US taxpayers to properly report such assets in their tax returns and to provide the IRS with the means to detect noncompliance. Government of the United States, Internal Revenue Service. Foreign Account Tax Compliant Act. <https://www.irs.gov/businesses/corporations/foreign-account-tax-compliance-act-fatca>

<sup>8</sup> Global Forum on Transparency and Exchange of Information for Tax Purposes. 2014. *Automatic Exchange of Information: A Roadmap for Developing Country Participation, Final Report to the G20 Development Working Groups*. 5 August 2014. <http://www.oecd.org/tax/transparency/global-forum-AEOI-roadmap-for-developing-countries.pdf>

**“Implementing the Common Reporting Standard for automatic exchanges requires some effort and costs on the part of individual participating jurisdictions.”**

### Box 2: Implementing the Common Reporting Standard

Implementing the standard in each jurisdiction involves four key steps done in any order or in parallel:

1. **Translate the reporting and due diligence requirements into domestic law.** Jurisdictions will need to set rules that require financial institutions to report information and follow due diligence procedures consistent with the standard. The required reporting and due diligence procedures—which are very similar to the United States’ Foreign Account Transparency Compliance Act (FATCA)—are described in detail in the standard, and can be used as a template for formulating domestic rules.
2. **Select a legal basis for the exchange of information.** Many jurisdictions already have legal instruments in place that allow automatic exchange under the standard, including bilateral double tax treaties and the Multilateral Convention on Mutual Administrative Assistance in Tax Matters. At the administrative level, automatic exchanges typically require separate agreements between competent authorities of participating jurisdictions to activate and “operationalize” the automatic exchange. These agreements specify the information to be exchanged and deal with practical issues such as the time and format of the exchange. The standard contains model competent authority agreements (both bilateral and multilateral) that can be used for exchanges under the standard.
3. **Prepare the administrative and information technology infrastructure required to collect and exchange information under the standard.** The standard includes a transmission format to be used for exchanging information between jurisdictions, virtually identical to the structure and content for FATCA. Both schemas have been developed in close cooperation with financial institutions, many of which are now familiar with their content and operation.  
 In 2016, the participants of the Tax Commissioners’ meeting at the Organisation for Economic Co-operation and Development Forum on Tax Administration (FTA) committed to the successful implementation of automatic exchange of financial account information, and agreed to a number of actions including a Common Transmission System designed to allow the exchange of tax information in a secure environment. This system will be a critical resource for all countries in terms of implementing their commitment to Automatic Exchange of Information, as well as other tax information exchanges such as Country-by-Country Reports (see later comments). At the request of the FTA, the Organisation for Economic Co-operation and Development is selecting a service provider to build and run this secure, encrypted common system for bilateral exchanges, which will be in place for the first exchanges under the Common Reporting Standard in September 2017.
4. **Introduce the necessary safeguards to protect confidentiality and taxpayer data.** The standard contains detailed rules on confidentiality and data safeguards which need to be in place both on a legal and operational level. The standard also includes a sample questionnaire that can be used by jurisdictions to identify areas in which they will need to make improvements.

Source: Global Forum on Transparency and Exchange of Information for Tax Purposes. 2014. *Automatic Exchange of Information: A Roadmap for Developing Country Participation, Final Report to the G20 Development Working Groups*. 5 August 2014. <http://www.oecd.org/tax/transparency/global-forum-AEOI-roadmap-for-developing-countries.pdf> for Tax Purposes website: (<http://www.oecd.org/tax/transparency/global-forum-AEOI-roadmap-for-developing-countries.pdf>)

#### *Implications of Implementing Automatic Exchanges for Developing Economies*

Clearly, implementing the CRS for automatic exchanges requires some effort and costs on the part of individual participating jurisdictions. However, as emphasized in the roadmap report these more immediate imposts need to be assessed

against the potential ongoing benefits from CRS adoption and implementation.<sup>9</sup>

- (a) **Detect tax evasion and concealed offshore assets:** AEOI can alert tax administrations of tax evasion previously unknown and undetectable, potentially raising substantial revenue.

<sup>9</sup> Automatic Exchange of Information: A Roadmap for Developing Country Participation, Final Report to the G20 Development Working Groups, 5 August 2014. pp. 9–10. (<http://www.oecd.org/tax/transparency/global-forum-AEOI-roadmap-for-developing-countries.pdf>)

- (b) **Deter future noncompliance:** Once in place, AEOI should deter tax evasion and encourage timely compliance of taxpayers who are aware that financial institutions will report directly to the tax administration.
- (c) **Supporting domestic synergies:** The standard relies on financial institutions reporting information to the tax administration for international reporting purposes. In this way, it is an extension of a growing trend among tax administrations worldwide to use third party information, particularly financial information, to assist with domestic tax compliance. The implementation of the standard may therefore provide an opportunity for tax administrations to enhance domestic compliance through ready access to financial institutions' account information on both domestic and foreign residents where this is not already the case.
- (d) **Enhanced reputation:** AEOI is the new global standard jurisdictions are expected to comply with as part of their responsibilities towards the global financial system. Observing the standard demonstrates a continuing commitment to transparency, and to tackling tax evasion and the flow of illicit funds. It is concrete evidence of a jurisdiction's commitment to improve both domestic and international tax compliance, and indicative of the quality and capacity of its institutions.

To assist developing countries, considerable support is being provided by international organizations, the Global Forum, regional tax bodies, and advanced economies. In addition, the establishment of a Common Transmission System, as noted in Box 2, should significantly simplify automatic exchanges for participating jurisdictions, minimizing their ongoing operational costs.

As of July 2016, over 100 jurisdictions have committed to implement the new standard on AEOI, with the first such exchanges due to begin by 2017.<sup>10</sup> For many jurisdictions, the key to this commitment has been their ability and willingness to join the Multilateral Convention on Mutual Administrative Assistance in Tax Matters,<sup>11</sup> thereby not having to negotiate bilateral agreements. Following implementation, there will be a regular flow of automatic exchanges of financial account data between participating jurisdictions which is expected to greatly enhance their ability to detect and deter tax evasion.

ADB members from Asia and the Pacific who are currently members of the Global Forum are identified in Table 1. Out of the 48 ADB members from within Asia and the Pacific, only around half are members of the Global Forum, meaning that many others have yet to commit to promoting international tax transparency and cooperation by agreeing to adopt the international standard of EOIR. As some jurisdictions who are already members of the Global Forum have yet to commit to implement the new AEOI standard, the number of jurisdictions in the region who will benefit over the medium term from automatically receiving information from tax authorities in other jurisdictions could be even less than one half, unless expeditious action is taken to engage with the Global Forum.

Within Southeast Asia, there have been calls for increased attention to this matter. For example, the Association of Southeast Asian Nations<sup>12</sup> (ASEAN) *Economic Community Blueprint 2025* draws attention to tax cooperation as one of the key elements in supporting regional competitiveness and expresses commitment to improving, among other things, the implementation of exchange of information processes in line with international standards.

ADB members in the region who are yet to engage with the Global Forum are strongly encouraged to give this matter further

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<sup>10</sup> OECD. 2016. *Automatic Exchanges of Information: Status of Commitments*. <http://www.oecd.org/tax/transparency/AEOI-commitments.pdf>

<sup>11</sup> The original Convention on Mutual Administrative Assistance in Tax Matters (on which the current multilateral convention is based) was developed jointly by the Council of Europe and OECD in 1988 to promote international cooperation for better functioning of national tax laws, while respecting the fundamental rights of taxpayers. It was framed to provide all possible forms of administrative cooperation between states in the assessment and collection of taxes, particularly with a view of combating tax avoidance and evasion. This cooperation ranges from exchange of information to the recovery of foreign tax claims. The 1988 Convention was revised in 2010 primarily to align it to the new internationally agreed standard on transparency and exchange of information and to open it up to states which are not members of the OECD or of the Council of Europe. OECD. 2010. *The Revised Explanatory Report to the Convention on Mutual Administrative Assistance in Tax Matters as Amended by Protocol*. [https://www.oecd.org/ctp/exchange-of-tax-information/Explanatory\\_Report\\_ENG\\_%2015\\_04\\_2010.pdf](https://www.oecd.org/ctp/exchange-of-tax-information/Explanatory_Report_ENG_%2015_04_2010.pdf)

<sup>12</sup> The ASEAN member states are Brunei Darussalam, Cambodia, Indonesia, Lao People's Democratic Republic, Malaysia, Myanmar, the Philippines, Singapore, Thailand, and Viet Nam; The ASEAN Secretariat. 2015. *ASEAN Economic Community Blueprint 2025*. Jakarta. p. 17.

**“The OECD reports that revenue losses from BEPS were conservatively estimated at \$100 billion to \$240 billion annually, and these losses were not just confined to advanced economies.”**

**Table 1: ADB Members from Asia and the Pacific who are also Members of the Global Forum on Transparency and Exchange of Information for Tax Purposes**

ADB Members from Asia and the Pacific (28 October 2016)		
Armenia	India <sup>a</sup>	Nauru <sup>a</sup>
Australia <sup>a</sup>	Indonesia <sup>a</sup>	New Zealand <sup>a</sup>
Azerbaijan	Japan <sup>a</sup>	Pakistan <sup>a</sup>
Brunei Darussalam <sup>a</sup>	Kazakhstan	Papua New Guinea
People’s Republic of China <sup>a</sup>	Republic of Korea <sup>a</sup>	Philippines
Cook Islands <sup>a</sup>	Malaysia <sup>a</sup>	Samoa <sup>a</sup>
Georgia	Maldives	Singapore <sup>a</sup>
Hong Kong, China <sup>a</sup>	Marshall Islands <sup>a</sup>	Vanuatu <sup>a</sup>

<sup>a</sup> Denotes country has also committed to implement the new AEOI standard.

Sources: Asian Development Bank. Members. <https://www.adb.org/about/members>; Global Forum on Transparency and Exchange of Information. <http://www.oecd.org/tax/transparency/about-the-global-forum/members/> (both accessed on 28 October 2016).

consideration. ADB recognizes that, as an international financial institution with a mandate to pursue sustainable development, it has a role to play in reducing tax evasion and the erosion of the domestic tax base of developing member countries. ADB fulfils its role primarily by providing technical assistance to enhance the capacity and regional cooperation of tax authorities in member countries to enable them to meet global standards. ADB, as an observer on the Global Forum, has welcomed the Addis Tax Initiative and has agreed to strengthen its collaboration with other development partners to jointly contribute in achieving the initiative’s objectives. Pursuant to ADB’s policy on Anti-Money Laundering and Countering the Financing of Terrorism, ADB also commits to increasing and strengthening its collaboration and cooperation with the Financial Action Task Force.

## 2. The Base Erosion and Profit Shifting Project

### *What’s the problem?*

The past 2 to 3 decades have seen dramatic changes in many economies as a result of globalization. Technological advancements, the free movement of capital and labor, the shift in manufacturing bases from high to low cost jurisdictions, and the gradual lifting of trade barriers, are some of the many developments that have boosted foreign direct

investment in many economies—creating jobs, boosting growth, and lifting millions out of poverty. However, there have been a number of downsides, including in the area of taxation, where it is widely agreed that international tax rules have not kept up with the pace of change. As observed by the OECD:<sup>13</sup>

*“Globalisation has opened up opportunities for multinational enterprises to greatly reduce the taxes they pay. The use of legal arrangements that make profits disappear for tax purposes or allow profits to be artificially shifted to low or no-tax locations is referred to as Base Erosion and Profit Shifting (BEPS).”*

*International tax rules have not always kept up with developments in the world economy, and globalisation has increased the need for countries to cooperate to protect their sovereignty on tax matters.”*

The OECD reports that revenue losses from BEPS were conservatively estimated at \$100 billion to \$240 billion annually, and these losses were not just confined to advanced economies. Many developing economies have a substantial multinational enterprise presence, meaning they are also impacted. The impacts of BEPS are multifaceted. Governments suffer directly because tax revenues are reduced and, as a consequence,

<sup>13</sup> OECD. 2015. Taxing Multinational Enterprises. *Policy Brief*. Base Erosion and Profit Shifting, p.1 <http://www.oecd.org/ctp/policy-brief-beps-2015.pdf>

others must share a greater share of the tax burden. Or, as more likely the case in developing economies, essential services required by citizens are simply not provided. More broadly, BEPS-related actions weaken tax system integrity and undermine citizens' trust in government. The goal of the BEPS project is to restore trust and ensure fair competition among all actors, while maintaining the ability to eliminate double taxation.

### *The BEPS Action Plan*

In September 2013, G20 leaders endorsed a comprehensive plan developed with OECD members to address BEPS. The starting point for this work was an action plan that identified a series of domestic and international actions to address the problem and set timelines for the implementation. A project team was established by the OECD, and from 2013 to 2015 the OECD and G20 member countries developed the measures on an equal footing, with extensive engagement by interested developing economies and regional tax bodies. In addition, there was extensive consultation with stakeholders. The OECD reports that the BEPS project received more than 1,400 submissions from industry, advisers, nongovernment organizations, and academics. The project also held 11 public consultations.

In October 2015, the BEPS project delivered its final outputs covering all elements of the action plan to G20 finance ministers. In November 2015, G20 leaders endorsed the measures at a meeting held in Antalya, Turkey.<sup>14</sup> In so doing, the G20 leaders expressly called for an implementation framework that would be open for all interested countries and jurisdictions, including developing countries.

### *The BEPS Package of Measures*

As described by the OECD, the BEPS measures aim to close gaps in international tax rules that allow multinational enterprises to legally, but artificially, shift profits to low or no-tax jurisdictions. The measures seek to achieve this by (i) improving the coherence of tax rules across borders, (ii) tightening substance requirements, and (iii) ensuring increased transparency and certainty.<sup>15</sup> A summary prepared

by the OECD of the specific measures contained in the BEPS package is provided in Box 3.<sup>16</sup>

### *Implementing the BEPS Measures—The Inclusive Framework*

Responding to G20 leaders' request, the OECD and G20 members have developed what is termed as the "Inclusive Framework" that enables interested countries and jurisdictions to work with OECD and G20 members on an equal footing in developing standards on BEPS-related issues, and to review and monitor the implementation of the BEPS package. To join the framework, interested countries and jurisdictions are required to commit to the BEPS package and its consistent implementation, and to pay an annual BEPS associate fee. It is acknowledged, however, that the circumstances of developing economies vary significantly, and that the timing of implementation of any BEPS-related measures may differ as a result. A reduced fee may be applied to developing economies with significant resource constraints.<sup>17</sup>

As recently reported by the OECD Secretary General,<sup>18</sup> the inclusive framework's inaugural meeting was held on 30 June to 1 July 2016 in Kyoto, Japan. In addition to 46 members, OECD accession countries and G20 members have already committed to the BEPS package, 39 additional countries and jurisdictions have now joined the BEPS inclusive framework. This brings the number of members in the BEPS project to (86 as of 14 October 2016),<sup>19</sup> with an additional 19 countries and jurisdictions that attended the inaugural meeting likely to join the inclusive framework by year end. The Secretary General also noted that at the Kyoto meeting, many developing countries took the opportunity to identify their specific concerns and asked for assistance to address them that took account of their specific environments.

Some Asian countries attending the BEPS launch identified significant benefits they could obtain, in particular from country-by-country reporting and from the use of multilateral instruments to protect their tax base from treaty abuse. They were also pleased to see that the

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<sup>14</sup> G20 Leaders' Communiqué, Antalya Summit, 15-16 November 2015, para. 15, (<http://g20.org.tr/g20-leaders-commenced-the-antalya-summit/>)

<sup>15</sup> Footnote 13.

<sup>16</sup> OECD 2016. Inclusive Framework for BEPS Implementation. *Background Brief*. <http://www.oecd.org/tax/background-brief-inclusive-framework-for-beps-implementation.pdf>

<sup>17</sup> Footnote 17. p.4.

<sup>18</sup> OECD. 2016. *OECD Secretary General Report to G20 Finance Ministers in Chengdu, People's Republic of China*. Paris. 23 to 24 July. p. 8. <http://www.oecd.org/ctp/oecd-secretary-general-tax-report-g20-finance-ministers-july-2016.pdf>

<sup>19</sup> OECD.2016. Inclusive Framework Composition. <https://www.oecd.org/tax/beps/inclusive-framework-on-beps-composition.pdf>

**“The BEPS package addresses the tax challenges of the digital economy, and identifies the main difficulties it poses for the application of existing international tax rules.”**

### Box 3: Overview of the Base Erosion and Profit Shifting package

**Action 1:** The work addresses the tax challenges of the digital economy, and identifies the main difficulties it poses for the application of existing international tax rules. The report develops detailed options to address these difficulties, taking a holistic approach, and considering both direct and indirect taxation.

**Action 2:** The work on neutralizing the effects of hybrid mismatch arrangements develops model treaty provisions and recommendations regarding the design of domestic rules to neutralize the effect (e.g., double non-taxation, double deduction, long-term deferral) of hybrid instruments and entities.

**Action 3:** The work to strengthen the rules for controlled foreign corporations develops recommendations regarding the design of controlled foreign company rules.

**Action 4:** The work on limiting base erosion via interest deductions and other financial payments, develops recommendations regarding best practices in the design of rules to prevent base erosion through the use of interest expense (e.g., through the use of related-party and third-party debt to achieve excessive interest deductions or to finance the production of exempt or deferred income, and other financial payments that are economically equivalent to interest payments).

**Action 5:** The work to counter harmful tax practices more effectively, taking into account transparency and substance, revamps the work on harmful tax practices with a priority on improving transparency, including compulsory spontaneous exchange on rulings related to preferential regimes, and on requiring substantial activity for any preferential regime.

**Action 6:** The work to prevent treaty abuse, develops model treaty provisions and recommendations for the design of domestic rules to prevent granting of treaty benefits in inappropriate circumstances.

**Action 7:** The work to prevent the artificial avoidance of permanent establishment status develops changes to the definition of permanent establishment to prevent the artificial avoidance of permanent establishment status in relation to base erosion and profit shifting, including through the use of commissionaire arrangements and specific activity exemptions.

**Actions 8–10:** The work to assure that transfer pricing outcomes are in line with value creation including work on: (i) intangibles by developing rules to prevent BEPS by moving intangibles among group members; (ii) risks and capital by developing rules to prevent BEPS by transferring risks among, or allocating excessive capital to, group members; and (iii) other high-risk transactions, develop rules to prevent BEPS in engaging in transactions that would not, or would only very rarely, occur between third parties.

**Action 11:** The work to establish methodologies to collect and analyze data on BEPS, and the actions to address it develops recommendations regarding indicators of the scale and economic impact of BEPS, and ensures that tools are available to monitor and evaluate the effectiveness and economic impact of the actions taken to address BEPS on an ongoing basis.

**Action 12:** The work to require taxpayers to disclose their aggressive tax planning arrangements develops recommendations regarding the design of mandatory disclosure rules for aggressive or abusive transactions, arrangements, or structures, taking into consideration the administrative costs for tax administrations and business, and drawing on experiences of the increasing number of countries that have such rules.

**Action 13:** The work to reexamine transfer pricing documentation develops rules regarding transfer pricing documentation to enhance transparency for tax administration, taking into consideration the compliance costs for business.

**Action 14:** The work to make dispute resolution mechanisms more effective develops solutions to address obstacles that prevent countries from solving treaty-related disputes under mutual agreement procedure, including the absence of arbitration provisions in most treaties, and the fact that access to MAP and arbitration may be denied in certain cases.

**Action 15:** The work on developing a multilateral instrument to modify bilateral tax treaties provides an analysis of the tax and public international law issues related to the development of a multilateral instrument, enabling countries to implement measures developed in the course of the work on BEPS, and amend bilateral tax treaties.

Source: OECD. 2016. *Inclusive Framework for BEPS Implementation. Background Brief*. March. pp. 9–10.



**Table 2: ADB Members from Asia and the Pacific who are also Members of the Inclusive Framework for BEPS Implementation**

ADB Members from Asia and the Pacific (as of 14 October 2016)		
Australia	Hong Kong, China	New Zealand
Bangladesh	India	Pakistan
Brunei Darussalam	Indonesia	Papua New Guinea
People's Republic of China	Japan	Singapore
Georgia	Republic of Korea	Sri Lanka

Sources: OECD. <http://www.oecd.org/tax/beeps/inclusive-framework-on-beeps-composition.pdf> and ADB. <https://www.adb.org/about/members> (both accessed on 28 October 2016).

burden of developing countries of meeting the four minimum standards for BEPS implementation was less than they had expected—in particular, there is a deferral from the work related to introducing mandatory arbitration and peer reviews for developing countries on other aspects will be scheduled appropriately. With regard to costs, developing countries will face the issue of staff resources required for engagement (and displacement of other work), as well as the cost of attending global meetings and the annual financial subscription for membership. To ease this administrative burden, consideration is being given through the use of webinars and the approval of documents through “written” procedure (e.g., e-mail). It was stated that membership fees would not be collected in 2016, anticipating that provision for this would not be available in developing countries’ tax administration budgets.

To date, developing economies in Asia and the Pacific have been relatively slow to engage with the international processes put in place to ensure that further work on the development of BEPS measures are inclusive and effectively coordinated. As Table 2 shows, to date only 15 out of 48 ADB members in the region have joined the inclusive framework.

The ASEAN has also raised this matter as part of its tax agenda. At their last meeting held on 4 April 2016 in Vientiane, Lao People’s Democratic Republic (Lao PDR), ASEAN finance ministers and central bank governors endorsed six broad strategies of taxation action plans, including specific attention to BEPS issues, and tasked its Forum on Taxation to work out a detailed plan with timelines.<sup>20</sup>

The ADB acknowledges that the issues raised by BEPS are complex, and that many

developing economies in the region have both limited experience in dealing with such issues and limited technical resources to help prepare necessary reforms. In this respect, engagement with the inclusive framework offers developing countries potentially valuable opportunities to: (i) further develop their knowledge of the proposed measures; (ii) learn how other jurisdictions are approaching the individual pieces of work required to implement to BEPS measures; and (iii) contribute to the further standard-setting work required. Furthermore, four international organizations (International Monetary Fund, OECD, the United Nations, and the World Bank) have launched an initiative—the Platform for Collaboration on Tax—that seeks to assist developing countries achieve improved revenue mobilization outcomes in line with Sustainable Development Goals. Concerning BEPS, the platform is already pursuing a program of work designed to support developing countries to address BEPS-related issues that are briefly described in Box 4. However, to be of any value, these efforts need to be matched by country-driven commitment to reform.

## Conclusion

With over 100 jurisdictions now actively engaged in the development and implementation of new rules in critical areas of international taxation, the momentum for significant changes over the coming years is at an unprecedented level.

The significant changes brought about by the work of the international organizations and driven by the G20 presents an extraordinary opportunity

**“With over 100 jurisdictions now actively engaged in the development and implementation of new rules in critical areas of international taxation, the momentum for significant changes over the coming years is at an unprecedented level.”**

<sup>20</sup> ASEAN. 2016. Joint Statement of the 2nd ASEAN Finance Ministers’ and Central Bank Governors’ Meeting. Vientiane, Lao PDR. 4 April 2016. <http://www.asean.org/storage/2016/04/Joint-Statement-of-the-2nd-AFMGM-FINAL-clean.pdf>

“For the reasons outlined, it would seem in developing countries’ immediate interests to consider engaging with the BEPS and EOI processes, while at the same time taking advantage of the technical assistance offerings available.”

#### Box 4: Platform on Collaboration on Tax: Toolkits Being Prepared on Base Erosion and Profit Shifting-related Issues

- Tools to address the issue of a lack of access to comparable information needed for transfer pricing purposes, with supplementary work targeting the issue of mineral pricing;
- Report on the issues arising from the indirect transfer of assets, to identify policy options to tackle abusive cases, with particular references to developing countries;
- Toolkit to support developing countries implement transfer pricing documentation requirements;
- Toolkit aimed at strengthening capacity for effective tax treaty negotiations;
- Toolkit to support countries implement rules to address base-eroding payments between affiliates of multinational enterprises, in particular, payments of interest, royalties, management and service fees;
- Toolkit on developing rules to counter artificial profit shifting through supply chain restructuring; and
- Toolkit for assessing base erosion and profit shifting risks in high-risk or significant industry sectors.

Source: OECD. 2016. Inclusive Framework for BEPS Implementation. *Background Brief*. March. pp. 9–10.

for developing countries to improve the operation of their tax systems. Participating as a full member in the BEPS and Exchange of Information fora will help them to achieve strategic changes to their tax policy and administration within a supportive international environment and to win the benefits of increased revenues. There are costs, but these are small, and the international aid that follows could be significant.

For the reasons outlined, it would seem in developing countries’ immediate interests to consider engaging with the BEPS and EOI processes, while at the same time taking advantage of the technical assistance offerings available.

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*The Governance Brief was peer reviewed by Yuji Miyaki, public management specialist (taxation), Governance Thematic Group, Thematic Advisory Cluster, ADB; and Brian McAuley, consultant.*

Note:

In this report, “\$” refers to US dollars.



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