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The **BEPS** Monitoring Group

A global network of independent researchers

Tax Certainty

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Fair and Effective Taxation

Clear and Easy to Apply

deducted at source – e.g. on employees
consumption taxes
not so for self-employed and business

Uncertain – Based on Abstract Concepts

'income', 'residence', 'source'
needs common understanding, based on trust
undermined by 'tax planning'
detailed rules lead to complexity, more avoidance
'cooperative compliance' or 'sweetheart deals'?

Why the Focus on Tax Certainty ?

- “negative effects on investment and trade” (European Commission Working Paper).
- “the importance of providing greater tax certainty to taxpayers to support trade, investment and economic growth has become a shared priority of governments and businesses.” OECD (2017, p. 5)

What is the Evidence ?

- Evidence for a relationship between tax uncertainty and investment is mixed.
- “theoretical literature shows that the effects of tax uncertainty depend on many factors and in some cases the results are counterintuitive” (EU WP p. 20).
- “theoretical literature finds that the impact of uncertainty in taxation on investment is unclear” ...outcomes depend on the “assumptions made” (OECD).
- So whether tax uncertainty matters is ultimately an empirical question.
- How to identify and measure tax uncertainty ?

Identifying Tax Uncertainty

- Tax uncertainty has been identified as:-
- The volatility in effective tax rates (EU Paper).
- Uncertainty about ‘effective tax rates’ was the third most important influence on investment in a survey of 88 professionals (Devereux).
- Uncertainty in tax law – EU Paper refers to the “use of ambiguous language”, and “complexity in the tax code”
- “Unclear, vague or poorly drafted legislative provisions will lead to tax uncertainty” (OECD).
- Court cases (OECD)
- **Note**: Measures of effective tax rates are inherently ambiguous due to data and other issues at the firm level and country level.

Sources of Tax Uncertainty

- “Tax uncertainty can derive from several sources. Weaknesses of the institutional framework of tax policy, at domestic and international level, are the main drivers” (EU paper).
- **More important sources are:**
- a culture of opportunistic behaviour and systematic tax avoidance.
- changing business models, especially the rise of the digital economy (Google, Facebook, Airbnb, Uber etc)

Uncertainty in Corporate Income Tax and Investment

- A survey of 724 companies, found uncertainty in corporate income tax to be “important” but “not the most important factor” influencing investment” (OECD/IMF, 2017).
- Other surveys consistently rank tax factors as 3rd or 4th in locational choice (EY Attractiveness survey 2017) and 7th in 2016.
- One problem is that research cited assumes firms pay tax.
- Investment decision making may be focussed on creating options (Research & Development) although valuable, often does not result in taxable cash flows.
- Start ups do not make tax profit.
- Loss making firms and those with accumulated losses do not pay tax.

Complete Tax Certainty May Not be Desirable

- Complete tax certainty can never be achieved and is undesirable from a public interest perspective.
- The OECD advocate a reduction in tax uncertainty by ensuring “appropriate mechanisms for consultation on proposed or announced legislation and enhanced guidance”.
- But “consultation” can easily turn into lobbying.
- IMF/OECD and EU argue strongly for binding mandatory arbitration.
- This proposal was controversial in the G20 BEPS project (Action 14), opposed by India amongst others, so remained an ‘option’.
- Binding mandatory arbitration is often linked to the doctrine of ”legitimate expectations”.
- The combination of these two concepts could lead to severe restrictions on the power of states to reform aspects of their tax and regulatory regime for foreign direct investment.

European State Aid Cases and Uncertainty

- The three concepts of reducing tax uncertainty, binding arbitration, and the doctrine of legitimate expectations all feature in appeals of the Competition Directorate State Aid Cases.
- The US Treasury White paper states:
  "the U.S. Treasury Department has been a strong proponent of binding mandatory arbitration to more efficiently resolve disputes, and has worked with a group of countries, including Belgium, Ireland, Luxembourg, and the Netherlands, over the past year on developing a multilateral instrument to incorporate it into existing treaties".
- The summary Irish Government case states the Commission has "infringed the principles of legal certainty and legitimate expectations".
- The next section deals with proposals for international tax reform.

Tax Treaties

- **Complex Network of Bilateral Agreements**
  creates loopholes, e.g. `hybrid mismatches’
- **BEPS Multilateral Convention**
  could create common floor of basic anti-abuse provisions
  71 signatories so far, 1100 matched Covered Agreements
  However –
    USA not a party
    some treaties unlisted (e.g. Mauritius’ with Africa)
    many reservations
- **Reasons?**
  Caution? – cannot add reservation later
  Non-OECD/G20 states not involved in BEPS
- **OECD/G20 states should withdraw or explain their reservations**

Transparency

- **Country-by-Country Reporting for TNCs**
  Clear template for basic information
  But filing and dissemination complex
  CbCRs should be public
- **Disclosure of Tax Avoidance Schemes**
  EU Commission proposal 2017
  First measures aimed at cross-border schemes
  But should add:
    - up-front payments
    - penalties for enablers of failed schemes

Transfer Pricing Rules & Arbitration

- **Arm's Length Principle Does Not Work**
  'Independent Entity' is a fiction – no comparables
  Functional analysis is subjective, needs specialists
- **Need clear criteria for apportioning profit**
  'where activities occur and value is created'
  e.g. CCCTB
  systematised profit-split method
- **Arbitration is the wrong solution**
  total secrecy undermines public confidence
  preference for 'baseball' method shows arbitrariness
- **Clear and Public Criteria best way to reduce conflicts**