

PART 1 OF A REPORT TO G20 DEVELOPMENT WORKING GROUP ON THE IMPACT OF BEPS IN LOW INCOME COUNTRIES

JULY 2014



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EXECUTIVE SUMMARY

At the G20's request, the OECD is leading the development of a strategy to address base erosion and profit shifting (BEPS). The Development Working Group (DWG) has asked the OECD to draw together the experiences of developing countries and international organisations in a report (of which this is Part 1) on the main sources of BEPS in developing countries and how these relate to the OECD/G20 BEPS Action Plan ('the Action Plan') on this issue. Annex A of this report identifies the relative significance to developing countries of each of the 15 Actions contained in the Action Plan.

The findings of this report are derived from dialogue and consultation with developing countries, and the experiences of international organisations working with developing countries. Direct consultations with developing countries were held in February and March 2014 at events organised by the OECD (in Asia and Latin America), the African Tax Administration Forum (in South Africa) and the *Centre de rencontres et d'études des dirigeants des administrations fiscales* (in Paris). The report also draws on dialogue with developing countries at meetings of the Task Force on Tax and Development (in October 2013 and March 2014), the meeting of the OECD Global Forum on Tax Treaties (in September 2013) and the meeting of the OECD Global Forum on Transfer Pricing (in March 2014).

BEPS relates chiefly to instances where the interaction of different tax rules leads to some part of the profits of Multinational Enterprises (MNEs) not being taxed at all. It also relates to arrangements that achieve no or low taxation by shifting profits away from the jurisdictions where the activities creating those profits take place. The international nature of tax planning means that unilateral and uncoordinated actions by countries will not suffice and may actually make things worse. The Action Plan to address the issues that lead to BEPS is a collective international effort which stands to assist both developed and developing countries.

BEPS impacts on domestic resource mobilisation in developing countries. For some of the poorest countries, which rely very heavily on tax revenue from MNEs, BEPS has a particularly significant effect on vital tax revenues. The impact of BEPS on developing countries, however, extends beyond revenue. BEPS undermines the credibility of the tax system in the eyes of all taxpayers. If the largest and most high-profile taxpayers are seen to be avoiding their tax liabilities, confidence and effectiveness of the tax system is undermined.

It is important to recognise that the risks faced by developing countries from BEPS, and the challenges faced in addressing them, may be different both in nature and scale to those faced by developed countries. This means that BEPS actions for developing countries may need specific emphases or nuances compared to those most suitable for advanced economies.

Key findings

This report finds that **developing countries often face policy and other conditions that impact on their abilities to address base erosion and profit shifting**. In particular:

- Some developing countries lack the necessary legislative measures needed to address base erosion and profit shifting.

- Developing country measures to challenge BEPS is often hindered by lack of information.
- Developing countries face difficulties in building the capacity needed to implement highly complex rules and to challenge well-advised and experienced MNEs.
- The lack of effective legislation and gaps in capacity may leave the door open to simpler, but potentially more aggressive, tax avoidance than is typically encountered in developed economies.

Developing countries and international organisations identify **the following key BEPS issues as being of most relevance:**

- Base erosion caused by excessive payments to foreign affiliated companies in respect of interest, service charges, management and technical fees and royalties.
- Profit shifting through supply chain restructuring that contractually reallocates risks, and associated profit, to affiliated companies in low tax jurisdictions.
- Significant difficulties in obtaining the information needed to assess and address BEPS issues, and to apply their transfer pricing rules.
- The use of techniques to obtain treaty benefits in situations where such benefits were not intended.
- Tax loss caused by the techniques used to avoid tax paid when assets situated in developing countries are sold.
- In addition, developing countries often face acute pressure to attract investment through offering tax incentives, which may erode the country's tax base with little demonstrable benefit (included in this report, not as an integral part of BEPS, but of first order concern to developing countries that impacts on the tax base).

Interim conclusions

BEPS has the potential to considerably impact on domestic resource mobilisation in developing countries. The risks faced by many developing countries, however, may differ from those faced by more advanced economies. For these reasons, developing countries have highlighted some of the action items in the Action Plan are of more relevance than others. They have also identified a number of issues, such as tax incentives, that are of concern to them, but which are not addressed in the Action Plan.

Next steps

An expanded version of this report (Part 2 will be presented in September 2014) will set out how the DWG might assist developing countries meet the challenges of the most relevant BEPS issues they face. This report will:

- Confirm which of the 15 actions included in the Action Plan are of most relevance to developing countries and whose corresponding outcomes can be expected to benefit them.

- Discuss other BEPS-related issues not in the Action Plan, including wasteful tax incentives, the lack of comparability data in developing countries and tax avoidance through the indirect transfer of assets located in developing countries.
- Discuss capacity building initiatives that, in the developing country context, must go hand-in-hand with regulatory measures. This will include a discussion on actions needed to ensure that developing countries can fully benefit from the most relevant issues contained in the Action Plan and how specific BEPS actions may need to be adapted (for example simplified) or supplemented (for example with additional guidance) to ensure they are effective for developing countries.

SECTION 1: INTRODUCTION

At the 2013 St. Petersburg Summit, Group of Twenty (G20) leaders recognised that “developing countries should be able to reap the benefits of a more transparent international tax system, and to enhance their revenue capacity, as mobilizing domestic resources is critical to financing development”.

The G20 leaders endorsed the St. Petersburg Development Outlook, which committed the DWG to “review relevant work on base erosion and profit shifting (BEPS) during 2014 in order to identify issues relevant to low income countries (LICs) and consider actions to address them”.

The DWG has requested a report on the main sources of BEPS for LICs (and other low capacity countries, hereinafter ‘developing countries’), how these relate to the OECD/G20 BEPS Action Plan¹ (‘the Action Plan’) and how the DWG might assist them to meet those challenges. The DWG has invited the OECD², as the organisation responsible for the Action Plan, to lead the development of the report, working closely with the International Monetary Fund (IMF)³.

This is Part 1 of the report, which was discussed at the meeting of DWG in May 2014. It identifies the BEPS issues of most significance for developing countries. Part 2 of the report, which will be available for the DWG meeting in September 2014, will i) highlight the actions developing countries have taken, many with international support, that indicate there are opportunities to raise additional revenues from addressing BEPS issues and to create a more certain and stable investment climate for business and ii) set out how G20 can assist developing countries address the challenges posed by these BEPS issues.

Annex A describes each of the 15 actions identified in the Action Plan and sets out the relevance of each action to developing countries, based on the consultations and experiences described in the box below.

¹ At the request of the G20, the OECD developed an Action Plan to tackle BEPS in a comprehensive manner. The Action Plan was fully endorsed by the G20 Finance Ministers at their meeting of 19 July 2013 and by the G20 Leaders at their meeting on 5-6 September 2013, with a mechanism to enrich the Plan as appropriate.

² The report is prepared under the responsibility of the Secretariats and Staff of the mandated organisations. It should not necessarily be regarded as the officially-endorsed views of those organisations or their member states.

³ The DWG’s Terms of Reference states: “Tax and Development Secretariat will also work with other international and regional organisations to elicit the views of LICs, including the African Development Bank, African Tax Administration Forum, Asian Development Bank, Centre de Rencontre des Administrations Fiscales, Economic Commission for Latin America and the Caribbean, Inter-American Center of Tax Administration, UN Committee on Tax and World Bank Group”.

This report is based on:

- a) Direct consultations with developing countries at regional BEPS consultation events (involving Asian, Latin American and Caribbean, and Francophone countries) and the ATAF Consultative Conference on New Rules of the Global Tax Agenda (involving African countries).
- b) Consultations with developing countries at the Annual Meetings of the OECD Global Forum on Tax Treaties, the OECD Global Forum on Transfer Pricing, and the OECD Task Force on Tax and Development. The Co-Chairs' Statement of Outcomes of the Task Force on Tax and Development is contained in the Annex B below.
- c) The experiences of OECD, World Bank Group and EU from their Tax and Development Transfer Pricing Programmes. These are demand driven programmes so provide evidence from the developing countries of the issues they consider are highest priority and which they are currently trying to address. Assistance is being provided to Albania, Bangladesh, Burundi, Cambodia, Colombia, Ethiopia, Ghana, Honduras, Jamaica, Kenya, Nigeria, Peru, Rwanda, Seychelles, Tanzania, Thailand, Uganda, Ukraine, Vietnam and Zambia. Feedback from developing countries is also received at OECD Global Relations events.
- d) The findings of a questionnaire sent to the participants to the March 2014 Global Forum on Transfer Pricing and comments received on requests for public input in the context of the BEPS Project.
- e) Comments and information received from the IMF⁴.

Annex C contains a glossary of terms used in this report.

⁴ IMF (2014) provides an extensive account of current international tax issues for developing countries.

SECTION 2: WHAT IS BEPS?

BEPS refers chiefly to instances where the interaction of different tax rules leads to some part of the profits of MNEs not being taxed at all. It also relates to arrangements that achieve no or low taxation by shifting profits away from the jurisdictions where the activities creating those profits take place.

It should be stressed that such planning by large MNEs is rarely illegal. In some cases, it is simply a matter of exploiting the unintended mismatches between the rules on the taxation of MNEs put in place by different tax jurisdictions. In other cases, avoidance is possible because internationally developed principles have not kept pace with the global integration of the economy. No, or low, taxation is not a cause for concern per se, but it becomes so when it is associated with practices that artificially segregate taxable income from the activities that generate it. In these cases, what matters is when income from cross-border activities goes untaxed anywhere.

Approximately 25% of intercompany transactions entered into by Colombian taxpayers are with low rate tax jurisdictions.

Source: Task Force Presentation, 28 March 2014

BEPS is a global issue that requires global solutions. The international nature of tax planning means that unilateral and unco-ordinated actions by countries will not suffice and may make things worse. The current OECD/20 Project, designed to address the issues that lead to BEPS, is a collective international effort which stands to assist both developed and developing countries. It is important to recognise, however, that the risks faced by developing countries from BEPS, and the challenges of addressing them, may be different both in nature and scale to those faced by developed countries. For example, gaps in developing country tax legislation, together with low administrative capacity, are likely to mean that developing countries facing cruder or more aggressive tax avoidance than typically encountered in more advanced economies. BEPS solutions need to be developed and evaluated with such issues in mind and BEPS actions for developing countries may need specific emphases or nuances compared to those more suitable for advanced economies.

Crude tax avoidance in Nigeria:

...most often, the companies making the payments are unable to demonstrate that commensurate benefits were obtained for these payments.

Source: OECD Questionnaire, March 2014

In addition, there are issues that create significant base erosion and potential double non-taxation in developing countries but which are not identified in the Action Plan. For example, governments increasingly offer MNEs tax incentives (such as tax-free periods or 'tax holidays') and in the consultation process developing countries voiced some doubts about the benefits of these measures. This is a long standing concern for developing countries and an area where a considerable amount of work has been carried out by the IMF and the World Bank Group. As tax incentives have a direct impact on developing country tax bases, and can give rise to the non-taxation of profit or to taxation of profit at a low rate, it is important that this issue is considered alongside other developing country BEPS issues. Tax incentives are therefore included within the scope of this report.

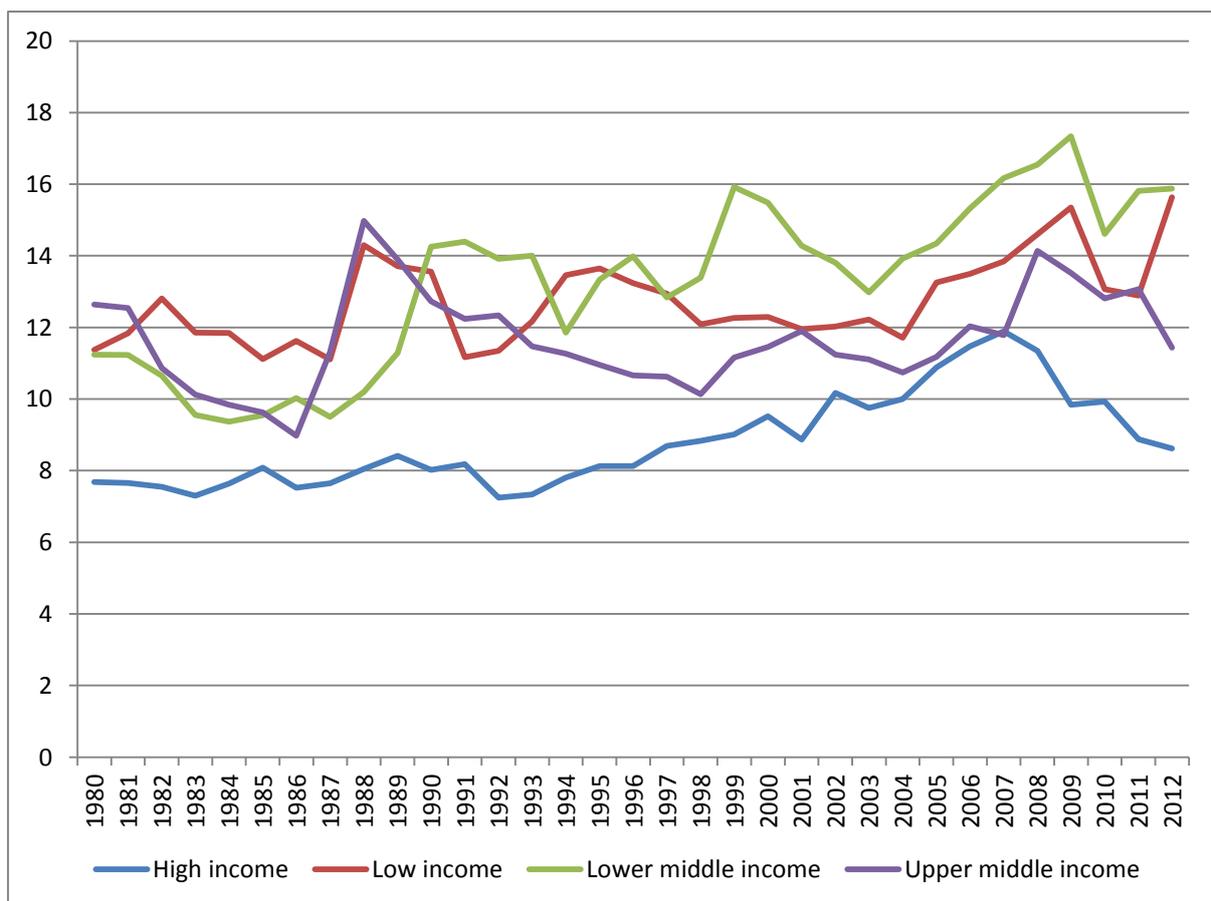
A further issue for developing countries, which was raised during the regional consultations, is the balance between source and residence taxation embodied in bilateral tax treaties modelled on the OECD and UN Model Tax Conventions. This is an issue of allocating taxing rights between two treaty partners. It is not a tax planning/avoidance issue and does not give rise to BEPS. It is thus outside the scope of the OECD/G20 BEPS Project and this report. However, it is recognised that this is an issue of significance for many developing countries, and that the OECD/G20 BEPS Project provides an opportunity to lay the ground for this legitimate debate. The BEPS consultations with developing countries have also highlighted the need to critically assess the costs and benefits of entering into tax treaties, and balance the policy objectives of revenue collection on the one hand and creating the right environment for foreign direct investment (FDI) on the other.

SECTION 3: BEPS AS A DOMESTIC RESOURCE MOBILISATION CONCERN

Moving towards a simpler, more equitable, transparent and broad based tax system has been a concern for developing countries for decades. Yet half of sub-Saharan African countries still mobilise less than 15% of their GDP in tax revenues, below the minimum level of 20% considered by the UN as necessary to achieve the Millennium Development Goals (UNDP, 2010) by 2015. Several Asian and Latin American countries fare little better. The urgency of domestic resource mobilisation, and the risk of BEPS, come together in sharp focus when developing countries' reliance on corporate income tax is considered.

As a share of all revenue, corporate income tax is more important in the poorest developing countries than in developed countries, as Graph 1 below shows.

Graph 1. Revenue from the corporate income tax as percentage of total revenue



Source: IMF (2014)

Extreme reliance on taxation of MNEs

- *Rwanda reports that 70% of its tax base comes from MNEs.*
- *In Burundi one company contributes nearly 20% of total tax collection. (Source: NSI, 2010)*
- *In Nigeria, MNEs represent 88% of the tax base. (Source: ATAF Conference, 18-19 March 2014)*
- *In Peru related party transactions account for 26% of GDP. (Source: Task Force Presentation, 28 March 2014)*

In some countries, reliance on MNE tax revenue is marked. This is not to downplay the importance of other pressing tax matters facing developing countries (such as the informal sector); rather, it is critical that developing countries are able to tax MNEs on the full profits that they earn in their jurisdictions according to clear rules.

Revenue loss from BEPS may be particularly important for resource rich developing countries. For these countries the taxation of natural resources is possibly the single biggest make or break fiscal concern in the next decade. MNEs dominate the extractive industries, and commonly export minerals to foreign related parties, making transfer

pricing a critical issue in the industry. BEPS risks in this sector therefore warrant particular attention.

The impact of BEPS on developing countries, however, extends beyond revenue from the taxation of MNEs. Companies operating only in domestic markets are at a competitive disadvantage if MNEs shift their profits across borders to avoid or reduce tax. More broadly, BEPS undermines the credibility of the tax system in the eyes of all taxpayers. If the largest and most high-profile taxpayers are seen to be avoiding their tax liabilities, confidence and effectiveness of the tax system is undermined. This is particularly important for developing countries as they face significant challenges with the taxing of “hard to tax” sectors, including small businesses (OECD, 2013).

The government of Zambia says that “it is losing as much as US\$2 billion annually to tax avoidance, and adds that the country’s mining industry is the biggest culprit”.

Source: Bloomberg, 25 November 2012

SECTION 4: BEPS IN THE DEVELOPING COUNTRY CONTEXT

The developing country experience of BEPS, and of countering BEPS, may be different from that of developed countries in six key areas.⁵

a) *The nature of cross-border tax planning may differ between developing and developed countries.*

Sophisticated tax planning structures may be less prevalent in, or of less pressing concern to, developing countries, where the lack of relevant and effective rules may leave the door open for much simpler tax planning strategies. Ineffective audit capacity may do little to discourage more aggressive and borderline tax planning practices. These differences in risks may need tailored approaches.

b) *Developing countries may lack the necessary legislative measures needed to address BEPS.*

A common issue for developing countries is incomplete legislation or legislation that is insufficiently targeted at the most important risks. Rwanda reports, for example, that its current transfer pricing rules are incomplete and are insufficiently effective to counter profit shifting. In many cases, rules can be easily circumvented. There is often more than one way in which profit can be shifted cross border, and legislation that closes one route will be ineffective if it leaves other routes open. For example, legislation that prevents profit shifting by means of transfer pricing will be of limited effectiveness if there is also no effective measure in place to prevent MNEs from introducing excessive interest-bearing debt into a country. Where such measures are in place, they may not be sufficiently robust.

“Delegates have to ask themselves whether they have all the legal instruments needed to adequately deal with base erosion”.
Ivan Pillay, ATAF Chair

Source: Moneyweb, 18 March 2014

c) *Accessing relevant information is often difficult.*

A common problem for developing countries is an inability to obtain the information they require from MNEs to adequately assess the risk of BEPS or to apply their rules to counter BEPS. This may be due to any or all of the following: i) lack of effective information-gathering rules, ii) poor compliance with such rules, or iii) limited capacity to implement and enforce them, iv) inadequate tools (such as e-filing systems) to capture information and then fully analyse it. Developing countries report that they face difficulties, for example, in obtaining information about the foreign operations of an MNE group often needed to fully assess the risk of tax loss. This is explored in more depth below.

⁵ On the importance and nature of international tax concerns for developing countries, see also IMF (2014).

d) Building and maintaining capacity to implement highly complex international rules that leave room for discretion in their application.

The number of tax and customs staff available for every 1000 citizens is 0.131 in Mozambique, 0.087 in Tanzania and 0.099 in Zambia in 2010. These 'tax staff per population ratios' are low compared to the world average of 0.82.

Source: CMI, 2011

Developing countries face specific challenges in applying a complex set of rules designed to counter cross-border international tax avoidance. First, tax administrations face competing priorities, often with woefully inadequate staffing. Second, many tax administrations are not competitive employers of skilled staff working on international tax avoidance issues, and there is a constant drain to the private sector, particularly the large accountancy firms. These constraints, combined with lack of experience, result in a well-known asymmetry when officials are confronted by well-advised large companies.

Finally, many developing countries may not have an established practice for settling disputes with large taxpayers conducting complex international transactions. The complex and fact-intensive nature of international tax rules means that disputes in developed countries are often settled by negotiation and compromise between the tax administration and taxpayer. This practice may not necessarily transfer well to the developing country context, where a culture of dealing with disputes in this way may be absent. In addition, the granting of wide discretion to tax auditors may open the door to corruption. Improving the effectiveness of dispute resolution while ensuring the integrity of the process needs to be explored in much further detail in the developing country context.

« Ils ont besoin d'être mieux armés pour répondre au rapport de force entre les multinationales et les administrations fiscales, souvent défavorable aux pays en développement ».

Source: CREDAF Event, 25 March 2014

Key messages from the Regional Consultations on BEPS concerning capacity issues

For developing countries, it is crucial that tax policy measures are capable of implementation, given the current constraints on capacity and access to information. Participants felt that implementation considerations should inform the development of the work on BEPS.

Source: Seoul Event, 20-21 February 2014

Africa must participate in the OECD/G20 BEPS Project and use the opportunity to shape the issues in the 15 Action points in this project. We should use the opportunity to ensure that sufficient attention is given to the different levels of readiness of African tax administrations and the resource and capacity limitations they have.

Source: ATAF Event, 18-19 March 2014

e) Need for political impetus and support for effective measures to counter BEPS highlighted in regional consultations.

The success of these measures will be determined not only by the technical accuracy of the solutions proposed, but also by the political consensus on the need for reforms.

Source: Bogota Event, 28 February 2014

An issue consistently raised by developing countries is the need to achieve political buy-in as a prerequisite to making the legislative changes and resource commitment required to counter base erosion and profit shifting. Lack of political awareness and commitment is cited by many developing countries as a major barrier to effectively introduce and apply rules to address BEPS issues.

f) The acute pressures on developing countries to attract investment can trigger a competitive 'race to the bottom'.

Although outside of the remit of the BEPS Action Plan, investment-targeted tax incentives granted to MNEs are eroding the tax base of developing countries, often with little demonstrable benefit. In 1980, 40% of sub-Saharan African countries offered tax holidays; in 2005, 80% did so (Keen and Mansour, 2009). This has been identified by developing countries as a key issue, and is discussed in more detail below.

Participants at the Regional Consultation on BEPS in Seoul agreed that, in the regional context, the OECD/G20 BEPS Project needs to reflect the balance between the encouragement of foreign investment and the need for domestic resource mobilisation for development.

Source: Seoul Event, 20-21 February 2014

Implications for developing countries

- Domestic rules to counter cross-border tax avoidance, and international standards and guidance, need to address the full range of potential risks.
- Rules also need to be implementable in the context of developing country resource and capacity limitations – this might mean they need to be simplified or more mechanical in nature, and allow for limited discretion.
- The development of international tax rules and guidance needs to take account of the limitations on access to information faced by developing countries.
- Improving the effectiveness of dispute resolution needs to be explored in the developing country context.
- BEPS issues for developing countries cannot be addressed in isolation from capacity issues and capacity building. It is critical that the BEPS actions take account of these capacity issues.
- Need for tax administrations, international and regional organisations, donors and NGOs to raise awareness of the significance of BEPS issues at developing country political levels.

SECTION 5: THE HIGH PRIORITY BEPS ACTION ITEMS FOR DEVELOPING COUNTRIES

Developing countries have identified the high priority BEPS Action Items, which are largely consistent across regions. This section of the report sets out the findings from consultations with developing countries (see Annex B) and from the experience of the IMF, OECD, World Bank Group and EU capacity development programmes with developing countries.

It should also be noted that although not specifically identified as a priority many developing countries recognise that the development of a multilateral instrument will be a useful mechanism for implementing the OECD/G20 BEPS Project measures particularly in the area of changes to double tax treaties.

The priority issues identified by developing countries are as follows:

a) Excessive or unwarranted payments to MNE affiliates – eroding the tax base of developing countries.

Developing countries regularly report that a variety of payments between companies in the same MNE group may unduly erode their tax base. They report that it is often difficult to assess whether such payments are for real value received, or whether they are excessive or unwarranted. These payments are typically for finance (e.g. interest payments), or for services, (e.g. management fees), or for intellectual property (e.g. royalty payments). Tax rules typically allow a deduction for such payments in arriving at the profit subject to tax, which means that excessive payments can inappropriately reduce the amount of profit on which tax is paid.

These types of payments arise in developed and developing countries but the risk of such payments eroding the tax base in developing countries may be greater as MNE affiliates in developing countries are generally recipients rather than providers of finance, services and intellectual property.

Developing countries have expressed specific concerns that their tax bases are eroded through payments of interest on loans. A company is usually financed (or capitalised) through a mixture of debt and equity. Excessive interest payments can arise if developing country taxpayers are burdened by excessive debt (known as “thinly capitalised”), or by an excessive price of debt. A deduction is normally made for interest in arriving at the tax measure of profit; so the higher the level of debt in a company, and thus amount of interest it pays, the lower the taxable profit.

Particularly common are payments to MNE affiliates for services provided by other members of the MNE group, such as for legal or IT services, or for management services or technical advice. For example, Mauritius reports that most of its transfer pricing issues arise where large management/technical fees are paid. Such payments are by no means always excessive, and may represent a fair return for valuable services provided. It is often difficult, however, for developing countries to obtain the full information needed to assess this.

58% of the developing country respondents to the questionnaire indicated that management fees and technical service fees regularly present transfer pricing enforcement issues in their country.

Source: OECD questionnaire, March 2014

Kenya reports that one of its key risks is transfers of locally developed intellectual property to low tax jurisdictions without compensation. A royalty is then charged for use by the Kenyan entity.

Source: Task Force Presentation, 28 March 2014

Royalty payments to MNE affiliates are also common. The ability to assess whether such payments are appropriate at all, or whether they are excessive in amount, again requires substantial information, and a high technical capacity.

A particular risk for resource-rich countries is the pricing of mineral export sales to MNE affiliates. Several countries have reported that they face challenges in ensuring that minerals are exported

at a fair price, again citing lack of data and information, and shortage of skilled capacity.

Implications for developing countries

- Need for effective and implementable rules to counter base erosion through the payment of excessive interest, including through excessive debt. (Addressed in Action 4 of the Action Plan, as described in Annex A below)
- Need for effective and implementable transfer pricing rules to counter base erosion through the payment of excessive royalties. (Addressed in Action 8 of the Action Plan, as described in Annex A below)
- Need for effective and implementable, and if necessary simplified, transfer pricing rules that enable developing countries to challenge excessive payments by MNEs in their countries to foreign related parties for management charges and service fees. (Addressed in Action 10 of the Action Plan, as described in Annex A below)

b) Developing countries face challenges due to new models for doing business, such as global value chains.

Globalisation has had an important impact on the way MNEs structure their business operations, bringing fresh challenges. The increasing mobility of capital and people, and the rapid adoption of technology to improve communications, has resulted in restructuring of MNE business models and operations. These changes are often based on centralised functions at a regional or global level rather than operations being managed within individual countries. Often referred to as “supply chain restructuring”, these practices are usually driven by business priorities, responding to efficiencies available from centralised planning, procurement and holding of intellectual property. However, they also make it easier to shift profits between tax jurisdictions giving rise to tax planning opportunities, and are often designed with tax minimisation in mind.

Kenya reports that some foreign companies operating in Kenya structure their business activities in a way to artificially avoid taxation.

Source: Task Force Presentation, 28 March 2014

Supply chain restructuring often involves the establishment of a central entrepreneurial company (the principal) in a low tax jurisdiction. Risks, such as bad debt, foreign exchange or inventory risks, are typically contractually transferred from, for example, a local distributor, to that principal, without moving the risk outside the MNE group as a whole. In such cases, the application of the arm’s length principle in transfer pricing rules can result in profits being shifted from the local

distributor to the principal. This ability to contractually shift risk between the members of an MNE (but not outside the MNE group as a whole) allows MNEs to plan where profits are reported, and thus tax paid.

Supply chain restructuring often goes hand in hand with the migration of valuable intellectual property to a centralised owner, often in a low tax jurisdiction, or where intellectual property is given favourable tax treatment. Where this happens, the income associated with that property also migrates, thus reducing the tax base.

Developing country tax administrations report that they are seeing many such restructurings, resulting in challenges arising from capacity shortfalls and information gaps. In some cases faced by developing countries, such restructurings are crude and abusive, with little or no substance behind them. In other cases, the complex nature of the restructuring means that testing the transfer pricing requires sophisticated analysis and comprehensive information in relation to both the resident taxpayer and the foreign principal. Successfully challenging such restructurings frequently involves the interaction of a number of tax rules – transfer pricing rules, tax treaties, the taxation of non-residents and rules concerning the transfer of intangible assets – all requiring strong technical capacity.

Implications for developing countries

- Need for effective and implementable transfer pricing rules that enable developing countries to address mismatches between where profit is recognised, and where it is truly earned. (Addressed in Actions 8, 9 and 10 of the Action Plan, as described in Annex A below)
- Need for effective rules that require MNEs to supply relevant information required to apply their transfer pricing rules. (Addressed in Action 13 of the Action Plan, as described in Annex A below)
- Need to update internationally developed principles to ensure developing countries can effectively tax foreign entities operating in their countries in line with the economic substance of their operations in those countries. (Addressed in Actions 1 and 7 of the Action Plan, as described in Annex A below)

c) Developing countries struggle to obtain the information they need to assess and address BEPS issues.

A major issue for developing countries is the ability to obtain information needed to assess the scale and impact of cross-border tax avoidance, and to take effective action to counter such avoidance.

Developing countries need data to adequately quantify tax loss from cross-border tax avoidance, and to pinpoint the sources and nature of such losses, as well as the effectiveness of measures introduced to counter them. The Action Plan recognises that this is an issue for developed and developing countries alike, and that work is needed to develop indicators of the scale and economic impact of BEPS. It is also acknowledged that tools are needed to monitor and evaluate the effectiveness and economic impact of the actions taken to address BEPS.

Developing countries also need to be able to obtain the information they require to select the most appropriate taxpayers for audit, and then to effectively check or challenge their transfer pricing. Most developing countries have reported that they face significant challenges in obtaining the information they need to apply their rules. In particular, they express concerns over the difficulties in

obtaining relevant information from taxpayers about the foreign members and operations of MNE groups.

Several developing countries have expressed strong support for the introduction of some form of country-by-country reporting. Country-by-country reporting was originally a transparency initiative promoted by civil society calling for the public disclosure of taxes and other financial data from MNE's in each of the locations in which they operate. More recently, the debate has been taken up by the G8 which called on the OECD to develop a common template for country-by-country reporting to tax authorities by MNEs, but not publicly disclosed. Many developing countries see the value of this work in helping them to assess the risks of profit shifting.

Implications for developing countries

- Need for the development of indicators of the scale and economic impact of BEPS, and tools are needed to monitor and evaluate the effectiveness and economic impact of the actions taken to address BEPS. (Addressed in Action 11 of the Action Plan, as described in Annex A below)
- Need for development of international standards and guidance on transfer pricing documentation and information reporting, including a common template for country by country reporting to tax administrations, that enable developing countries to obtain the information needed to assess the risk of transfer pricing abuse, and effectively address such risk. (Addressed in Action 13 of the Action Plan, as described in Annex A below)
- To expand the developments on transfer pricing documentation and information reporting to capture wider BEPS risks. (Addressed in Action 13 of the Action Plan, as described in Annex A below)

d) *Developing countries report that they lose out from treaty abuse.*

Around 3,000 bilateral tax treaties operate worldwide, and roughly 1,000 of these involve developing countries.

By way of background, most developing countries impose withholding tax on payments such as interest, management fees and royalties made by a resident taxpayer to a non-resident. These taxes are deducted from the payments by the payer, and then paid to the local tax authority. They are thus a tax on the foreign recipient of the payment. Withholding taxes in developing countries are usually between 10% and 20% of the payment amount. The effect of tax treaties, which usually override domestic legislation, is often to reduce that withholding tax to a lower rate or to zero.

Whilst developing countries generally agree that bilateral tax treaties have been effective in preventing double taxation, and support a predictable investment landscape, they are concerned about their misuse.

The concern is focused on the use of techniques (sometimes called "treaty shopping") to obtain treaty benefits (typically the reduction of withholding taxes) in situations in which such benefits were not intended.

Such techniques often involve the routing of payments of interest or royalties to an affiliate in a non-

Zambia sees transactions that are structured in a way to exploit the favourable terms found in a particular treaty. The effect is that Zambia loses out on withholding tax it would otherwise have been able to collect.

Source: OECD Questionnaire, March 2014

treaty country, through affiliates in a treaty country. Where this occurs, the country of the payer loses out on the withholding taxes that it would otherwise have been able to collect.

Estimates of lost withholding tax revenues for developing countries are hard to make. However, dissatisfaction among developing countries is possibly on the rise with Mongolia, for example, scrapping treaties with several jurisdictions because, according to the Mongolian Ministry of Finance, these arrangements are primarily used for tax avoidance by large extractive industry companies. The mining sector makes up more than 80% of Mongolia's exports and accounts for 30% of GDP.

Developed countries are beginning to take these concerns on board. The Netherlands, for example, is conducting a review of its tax treaties with developing countries, with a focus on anti-abuse measures. Mrs Lilianna Ploumen, Development Co-operation Minister, told the Financial Times: "By making use of loopholes in tax treaties in combination with differences between national tax rules, internationally operating companies can avoid paying tax. It means that poor countries miss out on tax revenues, funds they clearly need for matters such as infrastructure and education" (Houlder and Blas, 2013).

Implications for developing countries

- Need to identify the tax policy considerations that, in general, countries should consider before deciding to enter into a tax treaty with another country including carrying out a cost/benefit analysis of the tax treaty. (Addressed in Action 6 of the Action Plan, as described in Annex A below)
- Need for development of domestic rules, and treaty provisions, that counter the unintended use of treaties to avoid withholding taxes. (Addressed in Action 6 of the Action Plan, as described in Annex A below)

SECTION 6: OTHER HIGH PRIORITY BEPS ISSUES FOR DEVELOPING COUNTRIES

a) Developing countries face challenges in obtaining the data needed to apply the arm's length principle.

The international standard in transfer pricing, which is routinely incorporated in domestic transfer pricing rules, requires MNEs to price their related-party transactions in line with the pricing they would have used if they were conducting the same transaction with an unrelated party. Financial data about transactions between unrelated parties that are similar to the related party transaction (known as “comparable transactions”) is thus a prerequisite for countries to be able to effectively enforce their transfer pricing rules.

In Vietnam, data on actual transacted prices between independent parties (which has been the main focus of the tax authorities) is difficult to obtain and apply.

Source: EuropeAid

Developing countries frequently express concerns about the availability and quality of financial data on comparable transactions. This is reflected in the statement in the United Nations Practical Transfer Pricing Manual for Developing Countries (2012): “It is often in practice extremely difficult, especially in some developing countries, to obtain adequate information to apply the arm's length principle”.

A recent International Finance Corporation (IFC)/World Bank Group survey of local tax practitioners in 25 countries in the Europe and Central Asia (ECA) region found that 76% of the responses stated they often, very often or always, encounter difficulties in obtaining domestic comparable information (Loeprick, Cooper, and Christ, forthcoming). The issue of comparability is discussed in detail in a recent OECD discussion paper, *Transfer Pricing Comparability Data and Developing Countries* (OECD, 2014).

Implications for developing countries

- Stakeholders need to find approaches that address the lack of comparability data in developing countries.

b) Developing countries lose out from indirect transfer of assets.

This is a complex issue, but one which may have significant impact on the tax revenues of developing countries, especially (but not only) those countries where income from extractive industries are important. At the heart of the issue is the taxation of the profit made by the owner of an asset when that owner sells it (for example, the sale of a mineral licence). In some circumstances the country in which the asset is situated has the right under its domestic rules, and its treaties, to tax such profit. However, the IMF reports that the asset owner is sometimes able to avoid this taxation by means of an ‘indirect transfer’; that is, the sale of the shares in the company that owns the asset rather than the sale of asset itself, or the sale of the shares of another company that owns the shares of the first company.

Although many developing countries have rules that allow the taxation of a profit on such indirect transfers, challenges arise both in discovering the transaction in the first place, and collecting the tax from the foreign company that sold the shares.

Implications for developing countries

- Developing countries at risk need to enact effective rules to tax capital gains where ‘indirect transfers’ are used.
- Developing countries need to have sufficient information to identify indirect transfers. (Addressed in Action 13 of the Action Plan, as described in Annex A below)
- Developing countries at risk need effective procedures to tax the foreign company that has recognised the capital gains. (For example through membership of the Multilateral Convention on Mutual Administrative Assistance⁶)

c) Base erosion through wasteful tax incentives designed to attract investment – a major cause for concern.

In 2011, the OECD and other international organisations reported to the G20 DWG that tax incentives, including corporate income tax exemptions in free trade zones, continue to undermine revenue; where governance is poor, they may do little to attract investment – and when they do attract foreign direct investment (FDI), this may well be at the expense of domestic investment or FDI into some other country. Since then, the situation is likely to have deteriorated as more evidence has emerged of the proliferation of tax incentives designed to attract investors. Forgone tax revenues as a result of tax incentives ranged between 9.5% and 16% of GDP per year in the Eastern Caribbean Currency Union over a three year period, while the effect of tax incentive regimes on FDI appeared to be very modest (Chai and Goyal, 2008).

These figures need to be set alongside the most recent Investor Motivation Surveys, for example in Guinea, Rwanda, Tanzania and Uganda, which show that over 90 % of investors would have invested even if incentives were not provided (James, 2013).

Investor Motivation Surveys	
Countries Surveyed	Would have invested even if Incentives were <i>not</i> provided
Rwanda (2011)	98%
Uganda (2011)	93%
Guinea (2012)	92%
Tanzania (2011)	91%
Vietnam (2004)	85%
Thailand (1999)	81%
Mozambique (2009)	78%
Burundi (2011)	77%
Serbia (2009)	71%
Jordan (2009)	70%
Kenya (2012)	61%
Tunisia (2012)	58%

⁶ See: www.oecd.org/tax/exchange-of-tax-information/conventiononmutualadministrativeassistanceintaxmatters.htm

A study of 12 Western and Central African countries over the period 1994-2006 showed no relationship between tax holidays and investment (James and Van Parys, 2010).

Tax incentives ranked 11th out of 12 location factors in a survey of 7,000 firms in 19 African countries.

Source: UNIDO, 2011

The damage to the revenue base that erodes the resources for the real drivers of investment decisions — infrastructure, education and security — is compounded by the lack of transparency and clarity in the provision, administration, and governance of tax incentives in developing countries. The granting of tax incentives for investment in developing countries is often done outside of a country's tax laws and administration, sometimes under multiple pieces of legislation. The design and administration of tax incentives may be the responsibility of several different ministries (e.g., finance, trade, investment). Where various Ministries are involved, they may not co-ordinate their incentive measures (tax and non-tax) with each other or the national revenue authority, with the result that incentives may overlap, be inconsistent, or even work at cross-purposes. Administrative discretion in the management of incentives can seriously increase the risk of corruption and rent seeking.

The long-term costs of tax incentives include the economic burden that arises from international tax competition as competing countries put in place matching measures. This is of particular concern in developing countries where new measures are introduced or the existing measures are significantly augmented without properly assessing the likely reactions of other countries. This wasteful practice leads to the “race to the bottom”, as countries make themselves collectively worse off.

There is a need to assess the cost-benefit aspects of tax incentives, evaluate their effectiveness and convey the results to policymakers.

Source: ATAF Conference, 18-19 March 2014

Finally, tax incentives can create unintended tax-planning opportunities leading to revenue leakages. For example, existing firms can reconstitute themselves as “new” ones towards the end of their tax holiday periods so that they can continue to be tax-exempt. Likewise, companies can attempt to re-characterise certain activities so that they fall within the boundaries of qualifying business activities, such as R&D tax incentives. Similarly, tax incentives enable opportunities for profits and deductions to be artificially shifted across MNEs with different tax treatments either domestically or internationally. These tax planning opportunities are commonly exploited in both developed and developing countries; however, their ill effects are especially pronounced in developing countries that have limited capacity to detect and counter detrimental tax avoidance techniques.

Implications for developing countries

Tax incentives are not covered specifically in the Action Plan. However, action is required to:

- Develop better guidance on assessing the costs and benefits of tax incentives to inform policy formulation.
- Calculate the amount of revenue forgone which is attributable to tax incentives for investment, including revenue leakages due to unintended tax planning opportunities.
- Conduct periodic reviews of the impact of tax incentives by assessing the extent to which the incentives have the desired effects on investment and if these effects are achieved at a reasonable price.
- Improve transparency and governance of tax incentives for investment by i) providing tax incentives through tax laws only and by ii) consolidating them under the authority of one government body.
- Enhance regional co-operation to avoid harmful tax competition.

SECTION 7: PERSPECTIVES OF INTERNATIONAL ORGANISATIONS

The findings set out above are primarily derived from consultations with developing countries. They also reflect the experiences of the IMF, OECD and World Bank Group capacity development programmes with developing countries. A broadly consistent picture emerges from these various sources.

In particular, a direct source of evidence on the specific areas of international taxation that concern developing countries can be found in the requests for assistance received by the IMF. The Fund has provided assistance in these areas for many years, typically as part of wider advice in tax policy and administration. The box below provides a partial listing of international tax topics and (non-OECD) countries in which the Fund has provided demand-driven assistance in the last few years. In its recent paper focused largely on international tax concerns for developing countries (IMF, 2014), the Fund highlights four areas of special, though by no means exclusive, concern: interest deductions, treaty abuse, arms-length pricing and (not in the BEPS Action Plan) indirect transfers of interest – all of which are noted above.

Areas of recent IMF Technical Assistance in International Taxation

This has covered a wide range of topics and countries including:

- *Transfer pricing issues:*
Bangladesh; Burkina Faso; Cambodia; Colombia; Dominican Republic; Egypt; El Salvador; Ethiopia; Guatemala; Malawi; Mauritania; Mongolia; Nicaragua; Panama; Ukraine.
- *Issues related to provisions of double taxation treaties:*
Burkina Faso; Costa Rica; Dominican Republic; Egypt; El Salvador; Georgia; Honduras; Indonesia; Malawi; Mauritania; Mongolia; Nepal; Panama; Uganda.
- *Capital gains across borders:*
Mongolia; various AFR natural resource intensive countries.
- *Holding companies, related party debt, thin capitalization, others:*
Bangladesh; Cambodia; Colombia; Egypt; Malawi; Portugal; Romania; Uganda; Ukraine.

Source: IMF (2013)

SECTION 8: INTERIM CONCLUSION AND NEXT STEPS

Interim conclusions

This report finds that BEPS has the potential to considerably impact on domestic resource mobilisation in developing countries. The risks faced by many developing countries, however, may differ from those faced by more advanced economies. For example, the granting of wasteful tax incentives may be far more significant to developing countries than to developed countries. Developing countries may also face less sophisticated and more abusive tax planning structures. In addition, developing countries often have limited capacity, experience and skills to implement measures designed to counter BEPS, and face challenges in obtaining the information they require.

For these reasons, developing countries have highlighted that at the present time some of the action items in the Action Plan are of more relevance than others. Section 5 of this report highlights the main BEPS issues that developing countries have reported – focusing on base-eroding payments, treaty issues, new business models and transfer pricing documentation. Although outside of the OECD/G20 BEPS Project remit, tax incentives are a major cause of concern for developing countries. As developing countries start to address these issues, it is likely that some of the other issues identified in the Action Plan will assume greater significance and risk to their tax base and will need to be addressed.

Annex A below identifies which of the action items in the Action Plan are considered most relevant by developing countries in the light of these core concerns. It is clear from consultations with developing countries, however, that addressing BEPS needs to go beyond tax technical considerations: implementation is equally important.

Next steps

Part 2 of this report will be presented in September 2014 and will set out how the DWG might assist developing countries meet the challenges of the most relevant BEPS issues they face. This Report will:

- Confirm which of the 15 actions included in the Action Plan are of most relevance to developing countries and whose corresponding outcomes can be expected to benefit them.
- Discuss other BEPS issues not in the Action Plan but which have a direct impact on developing country tax bases, and can give rise to the non-taxation of profit or to taxation of profit at a low rate, and consider actions needed to ensure these issues are effectively addressed. These include the granting of wasteful tax incentives, addressing the lack of comparability data in developing countries and tax avoidance through the indirect transfer of assets located in developing countries.
- Discuss capacity building initiatives that, in the developing country context, must go hand-in-hand with regulatory measures. This will take account of the capacity building initiatives already underway between developing countries, international and regional organisations and other development partners to address BEPS related issues. It will include a discussion on actions needed to ensure that developing countries can fully benefit from the most relevant issues contained in the Action Plan and how specific BEPS actions may need to be adapted (for example simplified) or supplemented (for example with additional guidance) to ensure they are effective for developing countries.

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ANNEX A
ACTION ITEMS IN THE OECD/G20 BEPS ACTION PLAN OF MOST RELEVANCE TO DEVELOPING COUNTRIES

	Actions	Relevance
Action 1	<p>Address the tax challenges of the digital economy</p> <p>Identify the main difficulties that the digital economy poses for the application of existing international tax rules and develop detailed options to address these difficulties, taking a holistic approach and considering both direct and indirect taxation. Issues to be examined include, but are not limited to, the ability of a company to have a significant digital presence in the economy of another country without being liable to taxation due to the lack of nexus under current international rules, the attribution of value created from the generation of marketable location-relevant data through the use of digital products and services, the characterisation of income derived from new business models, the application of related source rules, and how to ensure the effective collection of VAT/GST with respect to the cross-border supply of digital goods and services. Such work will require a thorough analysis of the various business models in this sector.</p>	Medium
Action 2	<p>Neutralise the effects of hybrid mismatch arrangements</p> <p>Develop model treaty provisions and recommendations regarding the design of domestic rules to neutralise the effect (e.g. double non-taxation, double deduction, long-term deferral) of hybrid instruments and entities. This may include: (i) changes to the OECD Model Tax Convention to ensure that hybrid instruments and entities (as well as dual resident entities) are not used to obtain the benefits of treaties unduly; (ii) domestic law provisions that prevent exemption or non-recognition for payments that are deductible by the payer; (iii) domestic law provisions that deny a deduction for a payment that is not includible in income by the recipient (and is not subject to taxation under controlled foreign company (CFC) or similar rules); (iv) domestic law provisions that deny a deduction for a payment that is also deductible in another jurisdiction; and (v) where necessary, guidance on co-ordination or tie-breaker rules if more than one country seeks to apply such rules to a transaction or structure. Special attention should be given to the interaction between possible changes to domestic law and the provisions of the OECD Model Tax Convention. This work will be co-ordinated with the work on interest expense deduction limitations, the work on CFC rules, and the work on treaty shopping.</p>	Low
Action 3	<p>Strengthen controlled foreign companies (CFC) rules</p>	Low

	Develop recommendations regarding the design of controlled foreign company rules.	
Action 4	<p>Limit base erosion via interest deductions and other financial payments</p> <p>Develop recommendations regarding best practices in the design of rules to prevent base erosion through the use of interest expense, for example 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. The work will evaluate the effectiveness of different types of limitations. In connection with and in support of the foregoing work, transfer pricing guidance will also be developed regarding the pricing of related party financial transactions, including financial and performance guarantees, derivatives (including internal derivatives used in intra-bank dealings), and captive and other insurance arrangements. The work will be co-ordinated with the work on hybrids and CFC rules.</p>	High
Action 5	<p>Counter harmful tax practices more effectively</p> <p>Revamp 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. It will take a holistic approach to evaluate preferential tax regimes in the BEPS context. It will engage with non-OECD members on the basis of the existing framework and consider revisions or additions to the existing framework.</p>	Medium
Action 6	<p>Prevent treaty abuse</p> <p>Develop model treaty provisions and recommendations regarding the design of domestic rules to prevent the granting of treaty benefits in inappropriate circumstances. Work will also be done to clarify that tax treaties are not intended to be used to generate double non-taxation and to identify the tax policy considerations that, in general, countries should consider before deciding to enter into a tax treaty with another country. The work will be co-ordinated with the work on hybrids.</p>	High
Action 7	<p>Prevent the artificial avoidance of PE status</p> <p>Develop changes to the definition of PE to prevent the artificial avoidance of PE status in relation to BEPS, including through the use of commissionaire arrangements and the specific activity exemptions. Work on these issues will also address related profit attribution issues.</p>	High
Action 8	<p>Assure that transfer pricing outcomes are in line with value creation – Intangibles</p> <p>Develop rules to prevent BEPS by moving intangibles among group members. This will involve: (i) adopting a broad and clearly delineated definition of intangibles; (ii) ensuring that profits associated with the transfer and use of intangibles are appropriately allocated in accordance with (rather than divorced from) value creation; (iii) developing transfer pricing rules or special measures for transfers of hard-to-value intangibles; and (iv) updating the guidance on cost contribution</p>	Medium

	arrangements	
Action 9	<p>Assure that transfer pricing outcomes are in line with value creation – Risks and capital</p> <p>Develop rules to prevent BEPS by transferring risks among, or allocating excessive capital to, group members. This will involve adopting transfer pricing rules or special measures to ensure that inappropriate returns will not accrue to an entity solely because it has contractually assumed risks or has provided capital. The rules to be developed will also require alignment of returns with value creation. This work will be co-ordinated with the work on interest expense deductions and other financial payments</p>	Medium
Action 10	<p>Assure that transfer pricing outcomes are in line with value creation – Other high-risk transactions</p> <p>Develop rules to prevent BEPS by engaging in transactions which would not, or would only very rarely, occur between third parties. This will involve adopting transfer pricing rules or special measures to: (i) clarify the circumstances in which transactions can be recharacterised; (ii) clarify the application of transfer pricing methods, in particular profit splits, in the context of global value chains; and (iii) provide protection against common types of base eroding payments, such as management fees and head office expenses</p>	High
Action 11	<p>Establish methodologies to collect and analyse data on BEPS and the actions to address it</p> <p>Develop recommendations regarding indicators of the scale and economic impact of BEPS and ensure that tools are available to monitor and evaluate the effectiveness and economic impact of the actions taken to address BEPS on an ongoing basis. This will involve developing an economic analysis of the scale and impact of BEPS (including spillover effects across countries) and actions to address it. The work will also involve assessing a range of existing data sources, identifying new types of data that should be collected, and developing methodologies based on both aggregate (e.g. FDI and balance of payments data) and micro-level data (e.g. from financial statements and tax returns), taking into consideration the need to respect taxpayer confidentiality and the administrative costs for tax administrations and businesses.</p>	High
Action 12	<p>Require taxpayers to disclose their aggressive tax planning arrangements</p> <p>Develop 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 businesses and drawing on experiences of the increasing number of countries that have such rules. The work will use a modular design allowing for maximum consistency but allowing for country specific needs and risks. One focus will be international tax schemes, where the work will explore using a wide definition of “tax benefit” in order to capture such transactions. The work will be co-ordinated with the work on co-operative compliance. It will also involve designing and putting in place enhanced models of information sharing for international tax schemes between tax</p>	Medium

	administrations.	
Action 13	<p>Re-examine transfer pricing documentation</p> <p>Develop rules regarding transfer pricing documentation to enhance transparency for tax administration, taking into consideration the compliance costs for business. The rules to be developed will include a requirement that MNE's provide all relevant governments with needed information on their global allocation of the income, economic activity and taxes paid among countries according to a common template</p>	High
Action 14	<p>Make dispute resolution mechanisms more effective</p> <p>Develop solutions to address obstacles that prevent countries from solving treaty-related disputes under MAP, including the absence of arbitration provisions in most treaties and the fact that access to MAP and arbitration may be denied in certain cases.</p>	Medium
Action 15	<p>Develop a multilateral instrument</p> <p>Analyse the tax and public international law issues related to the development of a multilateral instrument to enable jurisdictions that wish to do so to implement measures developed in the course of the work on BEPS and amend bilateral tax treaties. On the basis of this analysis, interested Parties will develop a multilateral instrument designed to provide an innovative approach to international tax matters, reflecting the rapidly evolving nature of the global economy and the need to adapt quickly to this evolution.</p>	Low

The above are the action items in the Action Plan that developing countries have identified as being most relevant to their country. However, it is important to note that the new rules that are developed under the Action Plan will not in isolation address all of the base erosion and profit shifting issues faced by developing countries. Improved rules and access to information will assist but developing countries will also need to build the capacity of their tax administrations to implement the new rules and effectively use the improved access to information.

Furthermore developing countries will need to address the significant loss of revenue through the granting of wasteful tax incentives.

ANNEX B
SPECIAL MEETING OF THE OECD TASK FORCE ON TAX AND DEVELOPMENT⁷ ON
BASE EROSION AND PROFIT SHIFTING (BEPS) AND DEVELOPING COUNTRIES
AND SUMMARY OF THE BEPS CONSULTATIONS

CO-CHAIRS STATEMENT
Paris, March 2014

The OECD's Task Force on Tax and Development met in Paris, France, on 28 March 2014, to take stock of the ongoing efforts to consult with developing countries and understand their perspectives on the **Base Erosion and Profit Shifting (BEPS)** issues they are faced with. Governments, international and regional organisations, civil society and business representatives welcomed the significant progress made in this consultation process since the previous meeting in Korea in October 2013 and explored how to ensure that developing countries have an ongoing voice in the development of the work on BEPS to reflect developing country needs to better mobilise their domestic resources. This meeting was the culmination of a first round of consultations with the developing world, which we summarise below, together with future actions to ensure there is an ongoing dialogue with developing countries.

BEPS consultations with developing countries

As mandated by the G20 Leaders and reflected in the BEPS Action Plan of July 2013, developing countries have been extensively consulted on their priorities and ways to address BEPS challenges. This consultation process involved a combination of regional and global high-level policy dialogues. Following the Annual Meeting of the Global Forum on Tax Treaties of September 2013 and the Plenary Meeting of the Task Force of October 2013, 4 Regional Consultations were held in February and March 2014 (hosted by or in conjunction with regional tax organisations – CIAT, ATAF and CREDAF) to discuss BEPS issues with countries in Asia, Latin America, Africa and for francophone countries and to explore how the current work in the context of the OECD/G20 Project on BEPS should take those into account, with a particular focus on developing countries.⁸ Representatives of the UN Committee of Experts and IMF officials actively contributed to these events.

This first round of regional consultations was concluded with global meetings, where the main outcomes of the regional meetings were presented. The Annual Meeting of the Global Forum on Transfer Pricing was held on 26-28 March 2014, gathered over 330 senior tax officials from more than 110 jurisdictions. On 28 March 2014, Government officials were joined by representatives from

⁷ Co-Chaired by South Africa and the Netherlands, the Task Force is a multi-stakeholder advisory group set up to help to improve the enabling environment for developing countries to collect taxes fairly and effectively. This statement reflects the views of the Co-Chairs and not necessarily those of all stakeholders.

⁸ In three of these Regional Consultations, the Global Forum on Transparency and Exchange of Information for Tax Purposes also gathered countries views on the benefits and challenges for countries in the region in implementing the global standards on automatic exchange of tax information (AEOI).

civil society and the business community at the Task Force's Special Meeting on BEPS and Developing Countries. The final plenary session brought together the lessons learned from the intensive regional and global dialogue that has taken place over the past 6-8 months and proposed a number of ways forward.

Lessons learned from the ongoing consultations

The Task Force welcomed international efforts to gather effective input from developing countries on the work on BEPS. These meetings concluded that BEPS is of major significance for developing countries due to their heavy reliance on corporate income tax, particularly from Multinational Enterprises (MNEs). The different meetings were consistent in emphasising the following key messages:

- *Some items of the Action Plan were considered of higher immediate priority by developing countries.* These include limiting base erosion via interest deductions and other financial payments (Action 4), preventing tax treaty abuse and the artificial avoidance of PE status (Actions 6 and 7), transfer pricing, in particular base eroding payments (Actions 8, 9 and 10), and transfer pricing documentation and Country-by-Country Reporting (Action 13).
- *A number of other issues that are linked to, but not specifically included in, the Action Plan have been considered as of key importance in developing countries.* These were the granting of wasteful tax incentives which may erode the country's tax base with little demonstrable benefit and the significant difficulties developing countries face in obtaining relevant data, particularly comparable data for transfer pricing purposes.
- *Capacity building is one of the biggest challenges faced by developing countries.* The lack of effective legislation and gaps in capacity may leave the door open to simpler, but potentially more aggressive, tax avoidance than is typically encountered in developed economies. BEPS solutions for developing countries may need to be tailored to this reality, and concrete technical support will be needed to enable developing countries increase their capacity to improve their domestic resource mobilization.
- *Political support is critical to drive policy change that balances the encouragement of foreign direct investment with the need for domestic resource mobilisation.* All stakeholders have a role to play in increasing awareness about the importance of BEPS for developing countries and in ensuring that the required support is obtained from political decision makers.
- *Further engagement with developing countries is crucial to ensure that BEPS solutions are achieved at the global level.* The first round of regional consultations was very effective and it is important to continue the global dialogue on BEPS issues.

Developing country input received so far will be fed into the report for the G20 Development Working Group (DWG). This report, which is being prepared by the Task Force Secretariat in close cooperation with the IMF and other international organisations, is focused on the main BEPS issues and challenges faced by developing countries, how these are related to the BEPS Action Plan, and how the DWG might assist developing countries to meet those challenges.

Next steps

As Co-Chairs, we encourage international and regional organisations and all stakeholders to take further steps to ensure that developing countries' voices are taken into account in the international efforts to counter BEPS and strengthen domestic resource mobilisation. These steps include:

- Organising a further round of regional consultations towards the end of 2014 to take stock of the impact of BEPS outputs due by September 2014, and to input on the work under development with regard to the other outputs due later in 2015, ideally in conjunction with other planned BEPS meetings hosted by international and regional organisations.
- Make full use of existing mechanisms to channel input provided by developing countries into the OECD/G20 BEPS Project, e.g. through the comments to be provided by all interested parties on BEPS discussion drafts and public consultations; the direct participation of Government officials into the BEPS work at working group level; the publication of summaries reflecting discussions held during meetings on BEPS; and the use of questionnaires to inform the relevant working groups.

ANNEX C GLOSSARY

Arm's length principle

The international standard that OECD member countries have agreed should be used for determining transfer prices for tax purposes. It is set forth in Article 9 of the OECD Model Tax Convention as follows: where “conditions are made or imposed between the two enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly”.

Commissionaire

A commissionaire is an arrangement recognised under the European civil law concept of agency. Under civil law, a commissionaire can enter into sales contracts in its own name, but on behalf of the principal, where the commissionaire does not usually bind the principal. In theory the customer cannot sue the principal – there is no contractual relationship between the principal and the customer.

OECD/G20 Action Plan on Base Erosion and Profit Shifting (BEPS)

The Action Plan, published by the OECD in 2013, setting out a plan to provide countries with domestic and international instruments that will better align rights to tax with economic activity. The Action Plan (i) identifies actions needed to address BEPS, (ii) sets deadlines to implement these actions and (iii) identifies the resources needed and the methodology to implement these actions.

Permanent establishment (PE)

For the purposes of the OECD Model Tax Convention, the term “permanent establishment” means a fixed place of business through which the business of an enterprise is wholly or partly carried on.

The term “permanent establishment” includes especially:

- a) a place of management;
- b) a branch;
- c) an office;
- d) a factory;
- e) a workshop, and
- f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources

In addition, the term includes a “dependent agent” of a person in a country.

Under most treaties, a “permanent establishment” of a non-resident person in a country is required in order for that country to establish a right to tax any business profit earned by the non-resident person through the “permanent establishment”.

Tax treaty

This is a bilateral agreement made by two countries to resolve issues involving double taxation of income and capital.

Thin capitalisation

A company is typically financed (or capitalised) through a mixture of debt and equity. Thin capitalisation refers to the situation in which a company is financed through a relatively high level of debt compared to equity. Thinly capitalised companies are sometimes referred to as highly leveraged or highly geared.

Transfer pricing

This is the price at which an enterprise transfers physical goods, intangible property, or services to a related enterprise.

PART 2 OF A REPORT TO G20 DEVELOPMENT WORKING GROUP ON THE IMPACT OF BEPS IN LOW INCOME COUNTRIES

13 AUGUST 2014



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EXECUTIVE SUMMARY

This paper constitutes Part 2 of a two-part report to the G20 Development Working Group (DWG) on the impact of BEPS in low income countries. It builds on Part 1 of the report, which was presented to the DWG at its meeting in Hobart in May 2014¹.

The DWG has invited the Organisation for Economic Co-operation and Development (OECD) to write a report on the main challenges of BEPS in developing countries, how these are related to the Action Plan, and how the DWG might assist developing countries to meet those challenges. This report draws on the experiences of developing countries and the report reflects comments from the International Monetary Fund (IMF), given its body of work on international tax issues, with a particular focus on the special concerns and experiences of developing countries, and from the World Bank Group (WBG), United Nations (UN) and regional organisations².

The report is not intended to provide, and does not represent, a consensus view shared by these organisations.

The report identifies the highest priority BEPS issues faced by developing countries and sets out how the DWG could help. This means that the report is restricted to a discussion of issues, including capacity development concerns, that arise from the interaction between different tax rules or from arrangements that lead to no or low taxation by shifting profits away from the jurisdictions where the activities creating those profits take place. It should be recognised that this is only one of many challenges faced by developing countries as evidenced by the work of international organisations.

The 2011 report from the international organisations to the DWG (OECD, 2011) noted that a series of broader problems plague the revenue raising efforts of developing countries including corruption, the informal sector and various tax policy and administration concerns. This diagnosis remains true today and BEPS must be seen in the context of a range of priorities that each country faces. Nevertheless, for many developing countries, addressing BEPS is not a luxury item – one that can be delayed to when more advanced levels of development are reached. Reliance on corporation tax means addressing BEPS is an urgent domestic resource mobilisation matter – a bridge that must be crossed in lower and middle income countries, in combination with other pressing problems – and a strengthened capacity to address BEPS issues in turn strengthens effectiveness in other areas, including domestic tax avoidance.

The report outlines a number of recommendations on how the DWG can assist developing countries meet the challenges posed by BEPS, particularly the priorities identified in the Action Plan. The key messages and recommendations are as follows:

¹ The report is prepared under the responsibility of the OECD Secretariat. It does not represent the views of member states.

² The DWG's Terms of Reference state: "the report will be led by the OECD Tax and Development Secretariat, drawing on the views and expertise of the OECD Centre for Tax Policy and Administration (CTPA). ... The OECD Tax and Development Secretariat will work closely with and coordinate its work with the IMF, in order to benefit from the IMF's near-universal membership and expertise in domestic resource mobilisation in developing countries. ... The Tax and Development Secretariat will also work with other international and regional organisations to elicit the views of LICs."

- BEPS is an issue which harms developed and developing countries, arising from deficiencies of current international tax rules and standards. As a standard setter, the OECD is engaged in fixing these deficiencies involving all G20 countries on an equal footing. While it is recognised that no one size fits all, global solutions are needed to resolve global problems. It is essential that the OECD take the views and perspectives of developing countries into account when developing a new international tax framework.
- The OECD/G20 BEPS Project, which is responsible for the Action Plan, needs to ensure that BEPS solutions are relevant to, and effective for, developing countries. This means that developing countries must be fully engaged to ensure the solutions take into account the information and capacity gaps they frequently face. Some key concerns of developing countries have already shaped the Action Plan, such as revised transfer pricing rules that includes a template for country-by-country reporting to tax administrations, but the engagement of developing countries in the design of solutions needs to be stepped up. There are opportunities to put in place a more structured dialogue process, with clear avenues for developing countries to work together and directly input on the OECD/G20 BEPS Project. The OECD will strengthen the way it engages with developing countries over the coming months.
- Political level engagement on BEPS issues in many developing countries is at an early stage. G20 members, international and regional organisations, NGOs and other stakeholders can facilitate increased awareness of the importance of BEPS issues at developing country political levels, while recognising that BEPS may not be the highest priority issue in each case.
- G20 countries should analyse the spillover effects of changes to the design of their own tax systems on those of developing countries.
- The OECD, IMF, UN, WBG and regional organisations, where appropriate and they are in a position to do so, should assess how practical toolkits can be produced to help developing countries implement key BEPS actions regarding: for example, interest, services and royalties payments; the pricing of exported commodities; issues raised by business restructuring and accessing the information needed to assess and address BEPS. The toolkits will assist developing countries to address the highest priority BEPS issues. They will not create separate or alternative norms or standards.
- Part 1 of the report to the DWG shows that some of the key base erosion challenges faced by developing countries are not addressed in the OECD/G20 BEPS Project. The international and regional organisations can help the G20 to undertake further analyses on the lack of comparability data for transfer pricing, and on structures that indirectly transfer the ownership of an asset situated in a country in a way that avoids taxation by that country of profits arising from an increase in the value of that asset.
- Tax incentives, a major focus of work by the IMF, WBG and others for many years, are still a top priority concern for developing countries. Although outside the Action Plan, the DWG has already suggested further effort and recommendations will be required in 2015.
- The development of the Multilateral Instrument (Action 15) is still in its early stages but has the potential to be an important tool for developing countries that have a tax treaty network. This

instrument has the potential to be cost efficient to governments, while providing more certainty to foreign investors.

- The report recognises that capacity development on BEPS issues is critical. There has been extensive work by the international organisations in this area for many years, and the IMF, WBG and others have considerable experience. G20 members are active partners in this field. Some further recent international experience gathered under the auspices of the OECD's Task Force on Tax and Development suggests capacity building on BEPS issues achieves significant results, providing grounds for optimism as the Action Plan rolls out. The report proposes the DWG promotes and endorses the long-standing efforts of the international and regional organisations on BEPS issues, as well as some promising new initiatives such as the OECD's Tax Inspectors Without Borders (TIWB) through which G20 countries are gearing up support to developing country tax administrations.
- To guide their actions to address BEPS, DWG members can note some of the capacity development experiences from developing countries and international organisations. Lessons include the importance of approaching BEPS issues in the context of broader reform plans and development strategies; the role of regional organisations, civil society and business; and the importance of retaining skilled staff.

SECTION 1: INTRODUCTION AND BACKGROUND

At the 2013 St. Petersburg Summit, Group of Twenty (G20) leaders endorsed the St. Petersburg Development Outlook (G20, 2013), which committed the DWG to “review relevant work on base erosion and profit shifting (BEPS) during 2014 in order to identify issues relevant to low income countries (LICs) and consider actions to address them”.

In response to this commitment the DWG requested the OECD, working with other international and regional organisations, in particular with the IMF, to report on the main sources of BEPS for LICs and other low capacity countries (‘developing countries’), how those sources relate to the Action Plan and how the DWG might assist developing countries to meet those challenges.

Part 1 of this report was based on extensive dialogue and consultations with developing countries, and, in accordance with the DWG’s Terms of Reference, drew on the findings of the transfer pricing pilots undertaken by the OECD Task Force on Tax and Development, which featured in the DWG’s 2010 Multi-Year Action Plan. A key objective of the OECD’s participation in these pilots, undertaken in partnership between the European Union (EU), OECD and WBG, is for the OECD to gain a better understanding of the issues faced by developing countries in implementing internationally developed norms and standards. This is achieved by working directly with developing countries, and the EU and WBG.

Part 1 was discussed at the meeting of the DWG in May 2014. It reported that BEPS is a major concern for developing countries, and found that:

- While BEPS is a global issue, developing countries face specific policy issues and implementation challenges that are not always shared with developed countries;
- Some BEPS Actions are of more immediate relevance and concern to developing countries than others. Over the longer term, however, all BEPS Actions are likely to become important to developing countries as they work through their priority list and strengthen their tax systems accordingly;
- There are other base erosion issues, not covered in the OECD/G20 BEPS Project, which developing countries report are of immediate concern and which are already the subject of considerable technical assistance.

This paper constitutes Part 2 of the report, for discussion at the meeting of DWG in September 2014 in Perth, Australia. It builds on Part 1 and takes account of further consultations with developing countries and the comments received from the DWG meeting in May 2014.

This report proposes recommendations for the DWG to:

- Call on the OECD to ensure engagement with developing countries is stepped up so that BEPS solutions take account of specific capacity and political challenges faced by developing countries (in Section 2 below).
- Call on the OECD, IMF, UN, WBG and regional organisations, where appropriate and they are in a position to do so, to assess how they can assist developing countries address the challenges they face in relation to action items in the Action Plan (in Section 3 below).
- Call on the OECD, IMF, UN, WBG and regional organisations, where appropriate and they are in a position to do so, to assess how they can assist developing countries address the challenges they face from other BEPS related issues outside of the Action Plan (in Section 4 below).
- Welcome the work being carried out by international organisations in response to capacity development issues (in Section 5 below).

These recommendations are summarised in Section 6.

SECTION 2: STEPPING UP ENGAGEMENT WITH DEVELOPING COUNTRIES TO ADDRESS BEPS CHALLENGES AT TECHNICAL AND POLITICAL LEVELS

Part 1 of this report concluded that developing countries face challenges not always shared by developed countries. In particular it identified information and capacity gaps exacerbated by a lack of political awareness of these challenges. These have a number of implications that are discussed in this Section.

a) Engagement with developing countries to ensure the specific challenges they face are taken into account in designing BEPS solutions

BEPS is a global issue requiring solutions that are relevant for developing countries and effective in addressing their specific capacity and resource constraints. The design of BEPS solutions cannot ignore these constraints, and developing country views and perspectives must impact on BEPS solutions.

There has already been significant engagement between the OECD/G20 BEPS Project and developing countries which has already shaped the OECD/G20 BEPS agenda (see Box 1 below).

Box 1. Shaping the OECD/G20 BEPS agenda

Dialogue with developing countries has shaped the OECD/G20 BEPS agenda in several key areas:

- Work has begun in response to **concerns expressed by developing countries about the lack of quality comparability data** in their countries that can be used for transfer pricing purposes. Further details of this work are set out in Section 5 b) below.
- Revision of the Transfer Pricing Guidelines on documentation (Action 13) in response to developing country concerns that they face significant challenges in **obtaining the information they need to apply their transfer pricing rules**. This includes a **template for country-by-country reporting** to tax administrations of income, taxes and economic activity to meet the demands from many developing countries for the introduction of some form of country-by-country reporting. This will assist developing country tax administrations that have faced significant challenges in building a “big picture” view of a taxpayer’s global operations.
- New **guidance on safe harbours** for transfer pricing purposes have been produced in response to the concerns expressed by many developing countries that they face significant capacity issues in implementing highly complex transfer pricing rules and need some simplification measures. The guidance provides a basis for countries, especially developing countries, to design a transfer pricing compliance environment that makes optimal use of the limited resources available.
- In the context of the OECD/G20 BEPS Project, work is underway to develop transfer pricing rules to provide **protection against common types of base eroding payments**, such as service fees which were identified as a significant BEPS issue by developing countries during the BEPS consultation process.
- The **model anti-abuse provisions** that countries can include in treaties have been designed under the OECD/G20 BEPS Project to make it possible for tax administrations with limited capacity to administer them.

As the evidence base grows, indicating the importance of BEPS to the developing world, the time is right for the dialogue to be taken to a new level. There are opportunities to put in place a more structured dialogue process, with clear avenues for developing countries to work together and directly input into the work under the Action Plan. The OECD will strengthen the way it engages with developing countries over the coming months.

Recommendations

The DWG calls on:

1. The OECD/G20 BEPS Project to ensure that the outcomes of the Project take into account the specific challenges faced by developing countries, in particular in the highest priority Actions for developing countries (Actions 4, 6, 7, 10, 11, and 13).
2. The OECD to put in place a new structured dialogue process, with clear avenues for developing countries to work together and directly input into the OECD/G20 BEPS Project.

b) Need for stronger political awareness within both developing and developed countries

i) Political awareness in developing countries of the potential impact of BEPS on their country's tax base

The IMF regularly engages with its members on international tax issues, most intensely in its technical assistance work. Yet countries in the consultation process frequently reported the need to achieve political buy-in as a prerequisite to making the legislative changes and resource commitment required to counter BEPS. Many developing countries report that there is a lack of awareness at a political level on the need for action and reform. Box 2 below reports, as an example, the conclusions of Australia and New Zealand regarding the profile of BEPS in Pacific Island countries.

Box 2. Pacific Island countries have limited awareness of BEPS

In Australia and New Zealand's bi-lateral consultations with Pacific Island countries (PICs) most reported very little awareness of BEPS issues. Based on these consultations Australia and New Zealand see a need to engage further with PICs to build awareness of how BEPS affects broader domestic resource mobilisation efforts.

All stakeholders — G20 countries, international and regional organisations, civil society and donors — that have access to political levels in developing countries have a role to play in explaining BEPS risks and in bringing these issues to the attention of Ministers in government departments other than tax administrations, in particular Ministries of Finance.

Recommendations

The DWG calls on:

3. All stakeholders – G20 countries, international and regional organisations, civil society and donors – to raise awareness of the significance of BEPS issues at political levels in developing countries by holding high-level political dialogue on BEPS issues with developing country Ministers from Ministries of Finance and other relevant Ministries.

ii) Political awareness in developed countries of the potential spillover effects of changes to their tax systems on BEPS related issues in developing countries

The 2011 report from the international organisations to the DWG (OECD, 2011) recommended that developed countries undertake spillover analysis of the impact of any significant changes to their own tax systems on those of developing countries. The issue is further highlighted in Action 11 of the Action Plan, which includes the development of an economic analysis of the scale and impact of BEPS (including spillover effects across countries). In light of these developments, and the recent work undertaken by the IMF (IMF, 2014) on this topic, G20 countries should analyse the spillover effects of revisions made to their own tax systems on those of developing countries.

Recommendations

The DWG suggests:

4. G20 countries should analyse the spillover effects of revisions made to their own tax systems on those of developing countries.

SECTION 3: POTENTIAL ACTIONS TO ASSIST DEVELOPING COUNTRIES ON HIGH PRIORITY BEPS ISSUES

Section 3 and section 4 of this paper recommend that the DWG calls on international and regional organisations, where appropriate and in a position to do so, to assess how practical toolkits can be produced to assist developing countries implement key BEPS outcomes and to address the difficulties caused by a lack of comparability data. There is a clear need for this work but further discussion is required on how such toolkits should be developed, what they should cover, how the different international and regional organisations can assist in their development and the timelines going forward.

a) Base eroding payments between Multinational Enterprise (MNE) related parties

The profit-shifting risk of payments between related companies is one of the most frequently reported concerns of developing countries. Many consider that excessive or unwarranted payments by MNE taxpayers to foreign related companies represent a significant risk to their tax bases. They similarly report concerns about profit shifting through under-priced export sales to foreign related parties.

Risks arising from excessive or unwarranted payments are frequently reported in relation to payments of interest and royalties, or to fees paid for management or other services. Countries often find it difficult to apply the criteria contained in the current international tax rules to assess whether such payments are excessive or unwarranted.

Risks arising from under-pricing of exports to related parties occur in all industries, but are especially significant for some mineral and commodity products, where, again, international tax rules may be difficult to apply. This has led some resource rich countries to introduce rules intended to counter these specific risks. Box 3 below describes the rule introduced by Zambia, which is an example of rules sometimes described as the “Sixth Method”.

Box 3. Pragmatic adaptation: Zambia’s special rule on metals pricing

Zambia has introduced rules that apply to the sale of base metals or any substance containing base metals or precious metals between related parties. In such transactions the sale price for tax purposes will be broadly the monthly average quoted price on metal exchange markets.

The Action Plan addresses these types of risks under Actions 4 and 10. It is important that the design of BEPS solutions under these Actions takes account of the challenges that developing countries report in applying current international rules to these risks. The Zambian case illustrates the type of adaptation potentially of value and interest to many other countries together with tools that enable them to effectively implement BEPS solutions associated with these risks.

Recommendations

The DWG calls on:

5. The OECD/G20 BEPS Project to ensure that Actions 4 and 10 take into account developing country issues.
6. The OECD, IMF, UN, WBG and regional organisations, where appropriate and they are in a position to do so, to assess how practical toolkits can be produced to assist them implement rules to address BEPS issues relating to base eroding payments between MNE affiliates.

A toolkit might, for example, consist of:

- An explanatory note, describing how risks from base eroding payments between MNE affiliates arise.
- A paper on policy considerations and implications related to measures to counter tax loss arising from such payments.
- A description and analysis of regulatory options available, such as transfer pricing, thin capitalisation, anti-avoidance rules, BEPS special measures, as well as treaty measures, outlining potential advantages and disadvantages of each, in the light of country experiences to date.
- Model legislation and explanatory notes.
- Guidance on the administration of regulatory options (including governance), and practical auditing techniques.
- Supporting training materials.

b) Challenges created by new ways of doing business

As set out in Part 1 of the report the increasing mobility of capital and people, and the rapid adoption of technology to improve communications, has resulted in restructuring of MNE business models and operations.

Such restructurings offer the opportunity to contractually shift risk and valuable intellectual property from, for example, local distributors to a central entrepreneurial company (the principal) in a low tax jurisdiction. This ability to contractually shift risk and intellectual property between the members of an MNE (but not outside the MNE group as a whole) allows MNEs to plan where profits are reported, and thus tax paid.

Developing country tax administrations are seeing many such restructurings and challenging them frequently involves the interaction of a number of international tax rules—transfer pricing rules, tax treaties, the taxation of non-residents, and rules concerning the transfer of intangible assets.

The Action Plan recognises these rules have weaknesses that create opportunities for BEPS and these are being addressed by Actions 7, 8 and 9. It is important that the design of BEPS solutions through these actions takes account of developing country concerns and they are provided with the tools to enable them to implement the solutions. The box below proposes recommendations to address these issues.

Recommendations

The DWG calls on:

7. The OECD/G20 BEPS Project to ensure that BEPS Actions concerning the rules to counter artificial profit shifting through supply chain restructuring, for example the definition of a Permanent Establishment (Action 7), risk allocation and intangibles (Action 8 and 9), take into account developing country capacity limitations and information gaps.

8. The OECD, IMF, UN, WBG and regional organisations, where appropriate and they are in a position to do so, to assess how practical toolkits can be produced to assist developing countries implement rules to counter artificial profit shifting through supply chain restructuring.

A toolkit might, for example, consist of:

- An explanatory note, explaining how and why businesses restructure their supply chains, and the tax implications. This will include a description of the different supply chain models MNEs typically employ and guidance on how to identify a business restructuring has taken place.
- A paper on policy considerations in designing measures to ensure that MNEs that undergo, or have undergone, business restructuring pay the right amount of tax in each of the locations in which they operate.
- A description and analysis of the regulatory tools available to counter BEPS arising from business restructuring. These include transfer pricing, permanent establishment issues, residency issues, treaty measures, anti – avoidance rules and BEPS special measures.
- Guidance on the administration of regulatory measures, including how to assess the BEPS risks from the restructuring on risk assessment and practical auditing techniques.
- Supporting training materials.

c) Information needed to assess and address BEPS issues

A major issue for developing countries is the ability to obtain information needed to assess the scale and impact of cross-border tax avoidance, and to take effective action to counter such avoidance. Developing countries need data to adequately quantify tax loss from cross-border tax avoidance, and to pinpoint the sources and nature of such losses, as well as the effectiveness of measures introduced to counter them. This issue is being addressed by Action 11.

Again, it is important that the design of BEPS solutions through Action 11 takes account of developing country constraints and such countries are provided with the tools to enable them to implement the solutions.

In addition, despite many developing countries introducing transfer pricing documentation rules they still often face significant challenges in obtaining the information they require to select the most appropriate taxpayers for audit, and then to effectively check or challenge their transfer pricing and other cross-border practices.

These countries see significant value in the revised guidance on transfer pricing documentation rules and the country-by-country template being developed under Action 13 but have reported they will require supplementary tools and instruments to implement the guidance.

The box below proposes recommendations to address these issues.

Recommendations

The DWG calls on:

9. The OECD/G20 BEPS Project to ensure that Action 11 takes into account developing country issues.

10. International and regional organisations, where appropriate and in a position to do so, to assess how tools and materials can be developed to assist developing countries assess the risks they face from BEPS.

11. The OECD, IMF, UN, WBG and regional organisations, where appropriate and they are in a position to do so, to assess how practical toolkits can be produced to support the successful implementation by developing countries of a) assessment of BEPS risks, and b) effective transfer pricing documentation requirements that balance compliance imperatives with compliance costs. The toolkit might, for example, consist of:

- Model legislation and explanatory notes.
- Reviews of country information requirements, procedures and practices.
- Supporting training materials.

d) Challenges deriving from the abuse of treaties

Whilst developing countries generally agree that bilateral tax treaties have been effective in preventing double taxation, and support a predictable investment landscape, they are deeply concerned about their misuse.

The main concern is focused on the use of techniques (sometimes called “treaty shopping”) to obtain treaty benefits (typically the reduction of withholding taxes) in situations in which such benefits were not intended.

Action 6 addresses such misuse by designing model anti-abuse provisions that countries can include in treaties. The design of these provisions ensures the provisions are capable of being effectively administered by tax administrations with limited capacity.

Developing countries are also concerned that the interpretation of the treaty rules on Permanent Establishments allow contracts for the sale of goods belonging to a foreign company to be negotiated and concluded in the country by the sales force of a local subsidiary on behalf of that foreign company. This can lead to the profits from these sales not being taxable to the same extent as they would have been if the sales were made by the local subsidiary. Action 7 will develop changes to the definition of Permanent Establishments to address challenges posed by what is technically referred to as “commissionaire structures”.

A wider concern expressed by developing countries, and highlighted by NGOs in particular (McGauran, 2013), concerns the relative costs and benefits of entering into treaties. This raises both practical issues, such as the capacity of developing countries to ensure the treaty terms they negotiate are beneficial to the country, as well as policy considerations that countries should analyse before deciding to enter into a tax treaty with another country.

The box below proposes recommendations by the DWG to address these issues.

Recommendations

The DWG calls on :

12. The OECD/G20 BEPS Project to ensure that Actions 6 and 7 take into account developing country issues.

13. The OECD, IMF, UN, WBG and regional organisations, where appropriate and they are in a position to do so, to assess how to strengthen capacity development on treaty negotiation.

e) *Use of the multilateral instrument developed under Action 15*

Although the development of a multilateral instrument has not been identified as high priority by developing countries, the work by the OECD under Action 15 of the Action Plan to develop a multilateral instrument will minimize the cost and time required to modify bilateral tax treaty provisions. The multilateral instrument will be open to all countries and has the potential to be an important tool for developing countries to assist them counter BEPS issues and to provide more certainty to foreign investors.

Recommendations

The DWG calls on:

14. G20 countries to engage in dialogue with developing countries on the design and potential benefits of the Multilateral Instrument.

SECTION 4: POTENTIAL ACTIONS ON OTHER BASE EROSION ISSUES OF HIGH PRIORITY TO DEVELOPING COUNTRIES

a) *Tax loss on indirect transfer of assets*

Developing countries report that the profit made by the owner of an asset when selling it (for example, the sale of a mineral licence) is often not taxed in the country in which the asset is situated. Artificial structures are being used in some cases to make an ‘indirect transfer’; for example through the sale of the shares in the company that owns the asset rather than the sale of the asset itself.

The IMF reports some recent cases in developing countries of significant gains on indirect transfers of assets being untaxed (or with tax disputed) by the country where the underlying assets are located (see Box 4 below).

Box 4. Examples of indirect transfers

Mauritania: A Canadian company effectively acquired an interest in a large gold mining project [in Mauritania] from another Canadian company via a transaction in the Bahamas in 2010, with a potential capital gain of US\$4 billion. No tax was collected on the transaction in Mauritania.

Mozambique: In 2011 a change in ownership of mining projects in Mozambique was achieved through the sale, on the Australian stock market, of shares in the mining company holding interests in the projects. The value of the transaction was around US\$4 billion. No tax was collected on the transaction in Mozambique. In the case of the sales of shares in the exploration concessions in the Rovuma basin, the authorities have collected US\$1.1 billion in capital gains taxes in 2013-14. Changes were made to the tax code, on January 1, 2014, to ensure taxation of capital gains resulting from a direct or indirect transfer between non-residents of assets located in Mozambique (International Monetary Fund, 2014).

The UN Committee of Experts on International Cooperation in Tax Matters is also currently considering some of these issues in the context of tax treaties, as well as domestic law issues in the extractive industries.

Further work needs to be carried out on how domestic and international tax rules could be designed to address the indirect transfers of assets, in the developing country context.

Recommendations

The DWG calls on:

15. The OECD, in consultation with the IMF, to report on whether further analysis on this issue is needed to identify policy options to tackle abusive cases, with particular reference to developing countries.

b) Lack of data for transfer pricing comparability analyses

The international standard in transfer pricing, which is usually incorporated in domestic transfer pricing rules, requires MNEs to price their related-party transactions in line with the pricing they would have used if they were conducting the same transactions with unrelated parties. Financial data about transactions between unrelated parties (referred to as “comparable transactions”) is thus important for countries to be able to effectively enforce their transfer pricing rules.

Developing countries often lack financial data on comparable transactions³ effecting the application of transfer pricing rules to MNEs in all industries, but the lack of data on the pricing of certain natural resources is often particularly detrimental for developing countries. Some countries are starting to take measures to increase the data that might be used for transfer pricing purposes. Box 5 describes the approach taken by Kenya.

Box 5. Kenya expands data sources for transfer pricing analyses

Kenya has concerns regarding the availability and quality of financial data that might be used for transfer pricing purposes. To improve the data available it has introduced a requirement in its Companies Bill for statutory accounts to be filed with the central registry and to be made publicly available.

Developing countries recognise that measures such as those taken by Kenya above will assist, but they have also expressed an interest in:

- The development of additional tools (e.g. a template for carrying out searches for comparables), materials and training programmes on the use of available databases;
- The development of a toolkit to assist developing countries make appropriate use of foreign comparables (i.e. data on entities in a foreign country); and
- Work on alternative approaches to applying internationally agreed principles in the absence of reliable data on comparables, including work on safe harbours and approaches that operate in ways similar to the “Sixth Method” referred to in Section 3 a) above.

³ Measures to address this issue are discussed in the OECD document *Transfer Pricing Comparability Data and Developing Countries* (OECD, 2014).

Recommendations

The DWG:

16. Welcomes further work by the OECD and WBG to assess how practical toolkits can be produced to a) assist developing countries address difficulties in accessing comparables data and b) use approaches to apply internationally accepted principles in the absence of comparables (for example, safe harbour provisions).

A. Improving access to comparability data and the effectiveness of its use

A toolkit might, for example, consist of:

- An explanatory note, describing the role of comparables data in transfer pricing and implications of the inability to access such data.
- A description and analysis of measures developing countries might take to improve access to comparables data (such as expanding the scope and use of databases and the use of foreign comparables) or to reduce reliance on comparability data (including the use of measures and approaches such as the 'sixth method' that do not rely on the availability of such data).
- Model legislation and explanatory notes, where needed.
- Supporting training materials.

B. Safe harbours

A toolkit might, for example, consist of:

- An explanatory note, describing the key features of safe harbours and country approaches.
- A paper on policy considerations and implications of introducing a safe harbour regime.
- A description and analysis of regulatory options available, including developing country experience to date.
- Model legislation and explanatory notes.
- Guidance on the administration of safe harbours.
- Supporting training materials.

17. Calls on the OECD to commence a study on the feasibility of addressing the information gap on prices of some natural minerals sold in an intermediate form, e.g. mineral concentrate.

c) *Wasteful tax incentives*

Although outside of the Action Plan, Part 1 of this report raised concerns from developing countries about potentially wasteful tax incentives that erode the tax base with little demonstrable impact on investment. Many efforts are underway by governments, international and regional organisations and civil society to address these concerns. The IMF and WBG have analysed the problem and provided support to developing countries for decades.⁴ Recently, the OECD's Task Force on Tax and Development has proposed a set of *draft principles to enhance the transparency and governance of tax incentives for investment in developing countries* (OECD, 2013), that can be used as a diagnostic framework to analyse the problem in developing countries (see Annex 1). The G20 now has an opportunity to bring much of the existing knowledge together and to raise the profile. Using country-studies and focusing on governance and transparency, guidance could be developed for developing countries to better balance investment and tax revenue priorities.

Recommendations

The DWG welcomes:

18. A report (in 2015) on good practice in transparency and governance on tax incentives in developing countries from the IMF, OECD, UN and the WBG, using case studies, to better guide the developing countries in:

- Balancing investment and public revenue priorities.
- Estimating the cost of tax incentives, including revenue leakages due to unintended tax planning opportunities.

⁴ See for example, James (2013), Klemm and Van Parys (2009).

SECTION 5: CURRENT BEPS CAPACITY DEVELOPMENT ISSUES INVOLVING INTERNATIONAL ASSISTANCE PROVIDERS

Part 1 of this report relayed a clear message from developing countries that capacity development is critical to the successful implementation of measures to counter BEPS. The IMF, WBG and others have provided extensive support, including on international tax issues and tax incentives, and including through investment lending support, on strengthening tax policy and administration in developing countries for many years, with many positive results (OECD, 2011). More recently, International organisations have gathered specific evidence to show capacity development on BEPS issues can make a significant difference, including impacting on domestic resource mobilisation (see Box 6 below). This provides some grounds for optimism that BEPS solutions, with the right support, can be successfully implemented in developing countries as the BEPS Action Plan rolls out.

Box 6. Capacity development makes a difference

In 2011 the OECD, WBG and EU, began a programme of support for developing countries seeking to strengthen their transfer pricing rules and their implementation. Support initiatives are now in place in Colombia, Ethiopia, Ghana, Kenya, Peru, Rwanda, Vietnam and Zambia. Other country and regional projects are in the formative stages, including in Cambodia, the East African Community (EAC) and the Economic Community of West African States (ECOWAS) region. Key impacts of the programme include:

- Improved transfer pricing legislation and a new a transfer pricing decree in **Colombia**, aligned to international standards. Following transfer pricing adjustments made as a result of audits of MNEs, the Colombian tax administration has increased revenues from US\$3.3 million in 2011 to US\$5.83 million in 2012 (a 76% increase).
- Increased revenue collection in **Kenya**, from US\$52 million for year ended 30 June 2012 to US\$85 million for year ended 30 June 2013, following a training programme on advanced transfer pricing issues.
- New transfer pricing regulations in **Ghana** together with supporting guidance and a transfer pricing return schedule, complemented by a comprehensive skills-building programme with a newly established team of specialist transfer pricing auditors leading to the first transfer pricing audits in Ghana being started in 2014.
- Significantly improved capacity in **Vietnam** to enforce its transfer pricing rules, resulting in an increase in the number of audits conducted by the tax administration from one audit in 2012 to 40 audits in 2013, giving rise to transfer pricing adjustments of US\$110 million by the end of 2013.

With globalisation and a greater focus on BEPS, demand for capacity development assistance is increasing rapidly. G20 countries are already active in the tax and development cooperation area, including in addressing BEPS. Examples gathered by the G20 Presidency include: Australia, China, Germany, Japan, Korea, and Russia providing assistance to Timor-Leste, Democratic Republic of Congo, Ghana, Malaysia, African Tax Administration Forum (ATAF) member countries, and Europe and Central Asia (ECA) countries respectively. In addition, the UK is supporting the OECD and World Bank Group to deliver their transfer

pricing programmes. As further resources for support are deployed towards this area, the G20 can draw on some of the lessons learned from experience, described in the paragraphs below.

a) *Setting BEPS issues in the context of country-led reform plans and priorities*

The 2011 report from the international organisations to the DWG (OECD, 2011) noted that a series of problems plague the poorest countries including corruption, the informal sector and various tax policy and administration concerns. This diagnosis remains true today and is a useful reminder that, as the focus on international tax matters intensifies, BEPS issues must be seen as an issue that needs to be addressed in step with a broader range of reforms that each country undertakes, and in accordance with each country's policy agenda. For international assistance providers, Box 7 below provides some examples of tools and approaches developed to ensure that international support targets the most pressing needs.

Box 7. Approaching BEPS in context

The IMF's Tax Administration Diagnostic Assessment Tool (TADAT) is a diagnostic tool to help developing countries and international assistance providers see priorities in a comprehensive and strategic manner. In turn, this will help to set out how BEPS issues fit into wider reform contexts.

The WBG's IAMTAX is a benchmarking, diagnostic and monitoring tool which allows for a comprehensive assessment of tax administration performance. It is used for diagnosing a broad range of issues in a country and monitoring those over time.

Germany's Gesellschaft für Internationale Zusammenarbeit (GIZ) Good Financial Governance programme in Ghana supports a range of public financial management concerns. In this case, the support from OECD/WBG/EU on transfer pricing provides a contribution, and is designed and sequenced according to a broader set of related public financial management reforms and priorities.

b) *Regional organisations and BEPS capacity development issues*

Regional organisations have extensive membership and are increasingly influential in and beyond their regions. For example, ATAF now has 38 member countries, and has established a BEPS Working Group to lead an African approach to BEPS and give input into the OECD/G20 BEPS process.

Box 8 below describes steps already taken in Africa to increase collective action and co-operation, illustrating that regional organisations can act as powerful platforms to address BEPS capacity development issues.

Box 8. Acting regionally: mutual assistance among African countries

ATAF has developed the ATAF Agreement on Mutual Assistance in Tax Matters (AMATM). This multilateral instrument allows for the exchange of information, sharing of expertise, joint audits and investigations, and mutual administrative assistance among African countries. The AMATM has the potential to be a key instrument in the fight against BEPS in Africa.

In Latin America, the Inter-American Center of Tax Administrations (CIAT) is actively supporting the BEPS initiative. A BEPS workshop was co-sponsored in February 2014 in Colombia with a large number of Latin American and Caribbean (LAC) tax officials present. In October 2014 a follow-up to that event will be hosted in Spain during CIAT's Technical Conference. CIAT is also co-sponsoring seminars on transfer pricing in LAC, most recently in Trinidad and Tobago and Uruguay.

The Pacific Islands Tax Administration Association (PITAA) meeting in July 2014 provided an opportunity for senior tax officials to discuss BEPS issues relating to PICs.

c) Engaging with all stakeholders

Business and civil society both have key roles to play in the design and delivery of capacity development, and both stakeholders increasingly have a regular place in the dialogue on BEPS issues with governments in developing countries. They also have a role in complementing the efforts of international assistance providers. Business insights into the investment climate implications of BEPS, for example, can be important. Business can provide a unique source of highly valued industry knowledge to support actions to address BEPS.

Civil society has an equally important role to play in raising awareness of the significance of BEPS issues amongst developing country governments, international organisations and donors, and engagement by providers of support and local NGOs is to be encouraged.

Examples of promising partnerships are highlighted in Box 9 below.

Box 9. Working with business and civil society on BEPS issues in Zambia and Colombia

Colombia and Zambia are working with business and civil society, supported by the OECD/WBG/EU programme on transfer pricing.

Unilever is working with the Colombian Tax Administration (DIAN) and OECD/WBG to provide training on the consumer goods industry and its supply chain in 2014.

With the OECD, the mining industry is providing experts to help Colombia and Zambia to analyse the coal, copper and gold industry supply chains – all key BEPS risk areas.

The OECD and WBG are working closely with the Zambia Extractive Industries Transparency Initiative Secretariat on issues to improve transparency in financial reporting in Zambia.

d) Setting objectives and measuring results

Governments in developing countries are paying greater attention to setting out clear and measurable objectives for their own reform strategies on BEPS issues and from the support provided by international development partners. To support these efforts, the OECD and WBG have developed a results framework as a tool to discuss and define objectives with developing countries. For example, the programme with Ethiopia has a key objective of assessing the impact the introduction of safe harbour regulations has on creating a more certain investment climate and assisting the tax administration in ensuring its limited resources are used in the most effective way.

e) *Addressing institutional, organisational and individual needs*

The 2011 report to the G20 noted international assistance on tax matters should encompass institutional, organisational and individual issues in order to make a difference. This observation remains valid as international providers of assistance engage with more intensity on BEPS issues. New transfer pricing legislation, for example, will have little or no impact if an administrative structure for enforcing them does not exist. Similarly, the effectiveness of such rules will be severely impaired if auditors responsible for enforcing them lack the requisite skills. Capacity building thus needs to encompass a full spectrum of issues including: policy development; legislation and guidance; administrative structure and governance; risk assessment and practical auditing skills.

f) *Assessing and addressing BEPS issues holistically*

The BEPS Action Plan has highlighted the interactions between the various international tax rules that relate to BEPS and Part 1 of this report noted that capacity development on BEPS actions needs to encompass all BEPS issues of priority to developing countries.

The scope of capacity building programmes to assist developing countries on BEPS Actions should be designed to build effective regimes able to address all issues relating to BEPS. Each country context will vary, but where relevant may include transfer pricing, treaty issues, Permanent Establishment issues and thin capitalisation issues. Box 10 illustrates the point in the case of Nigeria.

Box 10. A holistic approach to addressing BEPS risks in Nigeria

Following a risk and needs assessment, Nigeria's Federal Inland Revenue Service (FIRS) identified that it faces significant risk to its tax base from i) abusive and inappropriate transfer pricing, ii) excessive interest payments out of Nigeria, iii) abuse of some of Nigeria's tax treaties, and iv) abuse of the definition of permanent establishments. Based on these findings the OECD/WBG/EU capacity development programme has been designed to address these concerns and to sequence different actions accordingly.

g) *Hands-on and focused support*

Many developing countries report that much of the training they have received over a number of years has focused on theory and principles. Such training has been useful as an initial step to raise awareness of the type of rules needed to counter base erosion and profit shifting, but there is high demand for a focus on the practical implementation of rules, skills building and peer-learning, centred on practical case studies and issues encountered by the tax administration. The IMF, WBG and others have, of course long recognised this and have extensive programmes of support in place. The transmission of skills and knowledge through hands-on support on real issues and cases is proving effective. The OECD's Tax Inspectors Without Borders (TIWB) described in Box 11 below is designed to respond to demand for such support by mobilising specialist audit skills.

Box 11. The OECD’s “Tax Inspectors Without Borders” (TIWB) Initiative

The OECD’s TIWB is a new project which deploys tax audit experts to work directly under the management and supervision of local officials in developing country tax administrations on audits, with a particular emphasis on international tax matters, including those covered in the Action Plan. TIWB programmes complement existing initiatives that focus on putting in place the regulatory and administrative building-blocks needed to counter base erosion and profit shifting, through a real-time, “learning by doing” approach to solve current audit issues while transferring knowledge and skills. TIWB assistance can cover direct and indirect tax audit issues including pre-audit risk assessment and case selection, audit investigatory techniques, audit cases involving transfer pricing issues, anti-avoidance rules, or sector-specific issues, relating for example to e-commerce, natural resources, financial services or telecommunications. TIWB programmes can be full-time, or involve periodic assistance, and there is no minimum or maximum period.

Most importantly, TIWB can assist with improving the quality and consistency of tax audits, achieving sustained improvements in tax audit skills, and a resulting rise in the level of voluntary compliance by taxpayers who see a strengthening of tax administrations’ ability to carry out their mandate. The project is in a pilot phase in 2014, with requests for experts from Albania, Ghana, Malawi, Papua New Guinea, Senegal and Vietnam currently being met by France, India, Italy, the Netherlands, South Africa and the United Kingdom.

h) Sustaining practical skills and knowledge

Competitive terms and conditions of employment are needed in tax administrations to ensure that officials with practical skills and knowledge are not lost to the private sector. For their part, providers of international assistance should be alert to the risks of building the practical skills of officials if they are only to be lost to the private sector. Box 12 below illustrates the measures Kenya has taken to ensure staff with specialist international tax knowledge and experience are retained.

Box 12. Retaining specialist skills in Kenya’s tax authority

The Kenyan Revenue Authority (KRA) has been successful in retaining the staff in its transfer pricing team. The KRA considers it has been able to achieve this through a combination of factors including providing market rate remuneration packages, strong leadership and a strong team ethic. The stability and experience developed within the team has assisted the KRA to build an effective transfer pricing regime to address BEPS related issues and achieve substantial year on year revenue increases from transfer pricing adjustments. The KRA reports that the IMF noted recently that the Kenyan tax administration was now well equipped to handle complex issues such as transfer pricing.

Recommendations concerning capacity development

The issues set out in this section align to the five actions set out in the G20 DWG guiding framework for response to capacity issues arising from the G20 agenda that was agreed at the G20 DWG meeting in Hobart on 8th to 9th May 2014.

Recommendations

The DWG promotes and endorses:

19. Capacity development programmes from international organisations on BEPS issues.
20. The OECD/WBG/business partnership to build industry knowledge in developing country tax administrations.
21. The OECD's 'Tax Inspectors Without Borders' initiative as a tool to build developing country capacity to implement BEPS solutions.
22. The proposed initiatives of regional organisations, and regional programmes, to assist developing countries on BEPS issues.

SECTION 6: CONCLUSION AND SUMMARY OF RECOMMENDATIONS

This report has set out how the DWG might assist developing countries meet the challenges of the most relevant BEPS issues they face, both the most relevant action items in the Action Plan and the most relevant other BEPS-related issues. However, this report comes in the mid-point of the OECD/G20 BEPS project and is by no means the final word on the impact of BEPS on developing countries. As BEPS solutions are finalised the recommendations and findings of this report will need to be reviewed and updated to reflect these solutions. Developing countries should be engaged throughout this process.

The table below summarises proposed recommendations for the DWG to address the BEPS issues of highest concern to developing countries, identified in Part 1 of this report.

Issue	Recommendation
Continuing dialogue with developing countries to ensure developing country issues are taken into account	<p>The DWG calls on:</p> <ol style="list-style-type: none"> 1. The OECD/G20 BEPS Project to ensure that the outcomes of the project take into account the specific challenges faced by developing countries, in particular in the highest priority Actions for developing countries (Actions 4, 6, 7, 10, 11, and 13). 2. The OECD to put in place a new structured dialogue process, with clear avenues for developing countries to work together and directly input into the OECD/G20 BEPS Project. 3. All stakeholders – G20 countries, international and regional organisations, civil society and donors – to raise awareness of the significance of BEPS issues at political levels in developing countries by holding high-level political dialogue on BEPS issues with developing country Ministers of Ministries of Finance and other relevant Ministries. 4. G20 countries should analyse the spillover effects of revisions made to their own tax systems on those of developing countries.
Development of toolkits to assist developing countries implement BEPS solutions	<p>The DWG calls on:</p> <ol style="list-style-type: none"> 5. The OECD/G20 BEPS Project to ensure that Actions 4 and 10 take into account developing country issues. 6. The OECD, IMF, UN, WBG and regional organisations, where appropriate and they are in a position to do so, to assess how practical toolkits can be produced to assist developing countries address base eroding payments

	<p>between MNE affiliates.</p> <p>7. The OECD/G20 BEPS Project to ensure that BEPS Actions concerning the rules to counter artificial profit shifting through supply chain restructuring.</p> <p>8. The OECD, IMF, UN, WBG and regional organisations, where appropriate and they are in a position to do so, to assess how practical toolkits can be produced to assist developing countries implement rules to counter artificial profit shifting through supply chain restructuring.</p> <p>9. The OECD/G20 BEPS Project to ensure that Action 11 takes into account developing country issues.</p> <p>10. International and regional organisations, where appropriate and in a position to do so, to assess how tools and materials can be developed to assist developing countries assess the risks they face from BEPS.</p> <p>11. The OECD, IMF, UN, WBG and regional organisations, where appropriate and they are in a position to do so, to assess how practical toolkits can be produced to support the successful implementation by developing countries of a) assessment of BEPS risks, and b) effective transfer pricing documentation requirements.</p>
Challenges deriving from the abuse of treaties	<p>The DWG calls on :</p> <p>12. The OECD/G20 BEPS Project to ensure that Actions 6 and 7 take into account developing country issues.</p> <p>13. The OECD, IMF, UN, WBG and regional organisations, where appropriate and they are in a position to do so, to assess how to strengthen capacity development on treaty negotiation.</p>
Use of the Multilateral Instrument	<p>The DWG calls on:</p> <p>14. G20 countries to engage in dialogue with developing countries on the design and potential benefits of the Multilateral Instrument.</p>
Addressing tax loss on indirect transfer of assets	<p>The DWG calls on:</p> <p>15. The OECD, in consultation with the IMF, to report on whether further analysis on this issue is needed to identify policy options to tackle abusive cases, with particular reference to developing countries.</p>
Addressing lack of transfer pricing comparability data	<p>The DWG:</p> <p>16. Welcomes further work by the OECD and WBG to assess how practical toolkits can be produced to a) assist</p>

	<p>developing countries address difficulties in accessing comparables data and b) use approaches to apply internationally accepted principles in the absence of comparables (for example, safe harbour provisions).</p> <p>17. Calls on the OECD to commence a study on the feasibility of addressing the information gap on prices of some natural minerals sold in an intermediate form, e.g. mineral concentrate.</p>
Addressing wasteful tax incentives	<p>The DWG welcomes:</p> <p>18. A report in 2015 on good practice in transparency and governance on tax incentives in developing countries from the IMF, OECD, UN and the WBG to better guide the developing countries in:</p> <ul style="list-style-type: none"> • balancing investment and public revenue priorities. • estimating the cost of tax incentives, including revenue leakages due to unintended tax planning opportunities.
Capacity development	<p>The DWG promotes and endorses:</p> <p>19. Capacity development programmes from international organisations on BEPS issues.</p> <p>20. The OECD/WBG/business partnership to build industry knowledge in developing country tax administrations.</p> <p>21. The ‘Tax Inspectors Without Borders’ initiative as a tool to build developing country capacity to implement BEPS solutions.</p> <p>22. The proposed initiatives of regional organisations, and regional programmes, to assist developing countries on BEPS issues.</p>

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ANNEX 1:

SELECTED DEVELOPING COUNTRIES EXPERIENCES SET OUT AGAINST THE OECD TASK FORCE ON TAX AND DEVELOPMENT PRINCIPLES TO ENHANCE THE TRANSPARENCY AND GOVERNANCE OF TAX INCENTIVES FOR INVESTMENT IN DEVELOPING COUNTRIES

Principle 1. Make public a statement of all tax incentives for investment and their objectives within a governing framework.

A public statement of the full extent of tax incentives in Nigeria is hard to achieve due to the complexity of the tax incentives framework. Tax incentives can also be introduced through laws (currently including as many as 15 acts and provisions), budget speeches, government notices, executed agreements, as well as Memoranda of Understanding between the government and businesses.

Principle 2. Provide tax incentives for investment through tax laws only.

In 2009, the Code of Fiscal Benefits harmonised most investment incentives in Mozambique. In 2013, as many as 17 laws and legislative acts were consolidated into the General Tax Code in Senegal, significantly improving transparency of the tax system.

Principle 3. Consolidate all tax incentives for investment under the authority of one government body, where possible.

In Ghana, as many as 10 organizations/agencies have the authority to recommend or grant tax incentives and exemptions.

Principle 4. Ensure tax incentives for investment are ratified through the law making body or parliament.

Proposed tax incentives measures in Zambia are announced through a budget speech delivered in Parliament by the Minister of Finance; and are debated, voted, and passed by Parliament.

Principle 5. Administer tax incentives for investment in a transparent manner.

The administration process for the Swaziland's Development Approval Order is opaque and includes discretionary eligibility criteria such as "beneficial to the development of the economy." The application process is long and time-consuming; it doesn't follow a set timeline.

Principle 6. Calculate the amount of revenue forgone attributable to tax incentives for investment and publicly release a statement of tax expenditures.

In Tanzania, in the 2013-2014 Budget Speech, the Government voiced a commitment to rationalise the existing investment incentives, in particular, to reduce tax exemptions from 4.3% of GDP in 2011-12 to a maximum of 1% by 2014, based on systematic analysis of revenues foregone.

Principle 7. Carry out periodic review of the continuance of existing tax incentives by assessing the extent to which they meet the stated objectives.

Impact evaluation of investment incentives in Mauritius prompted a move away from an investment regime of numerous and overlapping tax incentives towards the current simplified tax system.

Principle 8. Highlight the largest beneficiaries of tax incentives for investment by specific tax provision in a regular statement of tax expenditures, where possible.

The analysis of Ghana's tax expenditure landscape reveals that 15 largest "beneficiaries" take the vast majority, 93.2 %, of all VAT tax expenditures.

Principle 9. Collect data systematically to underpin the statement of tax expenditures for investment and to monitor the overall effects and effectiveness of individual tax incentives.

Not enough data is collected in Tunisia to allow for systematic cost-benefit analyses and simulation modelling of tax incentives. Integration and leverage of common inter-agency data is challenging due differences in the classification systems, which lack common definitions and structure.

Principle 10. Enhance regional cooperation to avoid harmful tax competition.

OECD is working with the SADC to strengthen investment policy framework at the regional level by defining common guidance across member states, including related to tax incentives. The project builds a SADC-wide mechanism to satisfactorily address the harmful tax competition.