BIAC THE VOICE OF BUSINESS AT THE OECD

William Morris
Chair, BIAC Tax Committee
13/15, Chauseee de la Muette, 75016 Paris
France

Achim Pross
Head, International Co-operation and Tax Administration Division, CTPA
Organisation for Economic Cooperation and Development
2 rue André-Pascal
75775, Paris, Cedex 16
France

Submitted by email: mandatorydisclosure@oecd.org

April 30th, 2015

Ref: OECD DISCUSSION DRAFT: MANDATORY DISCLOSURE RULES (BEPS ACTION 12)

Dear Achim

BIAC thanks the OECD for the opportunity to provide comments on its Discussion Draft on Action 12 (Mandatory Disclosure Rules) of the Base Erosion and Profit Shifting ("BEPS") Action Plan issued 31 March 2015 (the "Discussion Draft").

In the attached document, you will find a number of both general and specific comments, giving our feedback and concerns in response to the OECD's "building block" recommendations. BIAC supports the development and use of well targeted mandatory disclosure rules. As we state in the attachment, however, we are concerned that the options set out in the Discussion Draft could lead to overly-broad rules, substantially increasing the burden for taxpayers and tax authorities alike (especially in cross-border settings), and even create duplicative reporting requirements in some instances. We believe a more targeted set of "best practice" proposals would be more appropriate, as these could fully take into account both the many ways that tax administrations can gather better data (for example, and very importantly, through cooperative compliance relationships), as well as how the Action 12 proposals do (or should) interact with other parts of the BEPS project.

We very much hope that you find our comments useful, and we look forward to working with you on these important issues over the next few months.

Sincerely,

Will Morris, Chair, BIAC Tax Committee

General comments

1. Although BIAC supports the OECD's work on Action 12, we believe that the establishment of clear "best practices," rather than broader "building block" recommendations would be a more appropriate objective. BIAC believes that well targeted and designed Mandatory Disclosure Regimes can act as effective deterrents to aggressive tax avoidance, helping governments to legislate quickly and target specific arrangements.

2. We believe that a well-designed Mandatory Disclosure Regime should be tightly focused on instances of aggressive avoidance schemes, and should require disclosure from the promotors of such regimes. Maintaining a narrow scope will ensure that the administrative burden faced by the vast majority of compliant taxpayers is minimized where possible.

3. If the scope of the proposals is drawn too broadly, new Mandatory Disclosure Regimes will risk substantially increasing the compliance burden faced by taxpayers, and could swamp tax administrations with more information than they can effectively review, potentially reducing the possibility of targeting aggressive schemes.

4. We also note that through a number of other BEPS Actions, additional requirements will be placed on taxpayers to document and/or report transactions to tax administrations (for example, the OECD's proposals through Action 13 on Transfer Pricing Documentation). In some cases, such information will even be automatically exchanged by tax administrations, providing more data than ever before. We believe that the proposals made under Action 12 should assist countries in targeting specific situations of avoidance that seek to abuse specific rules, for example, the situations identified in Paragraph 238 of the Discussion Draft.

5. The Discussion Draft briefly refers to the important work done by the Forum on Tax Administration in the area of Co-operative Compliance. The report states that mandatory disclosure and Co-operative Compliance programs are both intended to improve transparency, risk assessment and ultimately, tax payer compliance. However, the Discussion Draft undermines the principle of a co-operative compliance relationship, by stating that mandatory disclosure rules can reinforce the effectiveness of a cooperative compliance regime. Under a Co-operative Compliance program, the tax payer and tax administration enter into a more open relationship, where the taxpayer shares additional information about its business and transactions. These programs form a deliberate part of a tax administration's risk management strategy. The quality and scope of information provided through such a relationship is much higher than under a mandatory disclosure regime. Mandatory disclosure regimes and Co-operative Compliance programs should be treated as distinct risk management strategies adopted by tax authorities. It would be more appropriate to provide exemptions from mandatory disclosure requirements to companies entering into co-operative compliance relationships.

6. The Discussion Draft does not make any recommendation in relation to the confidentiality of disclosures and how they would be shared among the countries. Clear guidelines will be required to ensure that information is protected and shared in an appropriate way. Transactions and

"schemes" reported under a mandatory disclosure regime should be protected by appropriate confidentiality provisions as some of the information reported is likely to be commercially sensitive. Much like the OECD's proposals under BEPS Action 13, disclosures should be shared between tax administrations rather than between the taxpayer and multiple tax administrations.

7. BIAC believes that any new mandatory disclosure regimes should be implemented on a forward looking basis (i.e. applying to new "schemes" or transactions entered into after the date of implementation. Such rules should not require the retroactive disclosure of transactions.

8. The European Commission ("EC") has announced proposals for a Tax Transparency Package, part of which would require the automatic exchange of tax rulings. As part of the proposed package, EU countries would be required to report every three months to all other Member States on all advance cross-border tax rulings and advance transfer pricing arrangements. Mandatory disclosure regimes should take into account how and if such rulings will be disclosed to other relevant jurisdictions to avoid duplication.

Limited period for full consultation

9. Due to the extremely short comment period and the need, in parallel, to comment on a number of additional consultation documents, BIAC has focused on high-level issues. The absence of comments on other sections of the Discussion Draft should not be considered an endorsement of the proposals contained therein.

Specific comments

The need for clear guidelines

10. BIAC recognizes the importance of establishing principles for implementing Mandatory Disclosure Regimes. The OECD's recommendations should be clear and easy to understand. Existing disclosure regimes do not always achieve these goals. The OECD should, therefore, provide guidance as to "best practices". This is crucial as countries looking to introduce a Mandatory Disclosure Regime will hopefully look to base their regime on such best practices. Non-best practices should be identified as such, and countries should be discouraged from adopting them.

Preventing duplication of disclosures

Multiple disclosure requirements the same transaction

11. BIAC believes that Mandatory Disclosure Regimes should consider existing reporting requirements to avoid duplication. A Mandatory Disclosure Regime that applies a "main benefit threshold" would likely be similar to any applicable GAAR. Applying such similar tests would risk creating duplicative reporting requirements for the same transaction. GAARs should already discourage taxpayers from entering into such arrangements. The main benefit or a main benefit threshold would also create an unacceptable level of uncertainty. In particular, applying two different regimes could result in double penalties for the same failure. That is, if a taxpayer does not consider the main purpose of the transaction to be the tax benefit, and therefore does not report

it, applying both a GAAR and a Mandatory Disclosure Regime could result in double penalties. At a minimum, the OECD should provide that penalties should not be applied more than once in relation to a particular transaction.

12. BIAC believes that information that is provided as part of the OECD's Transfer Pricing Documentation package should not be demanded again under a Mandatory Disclosure Regime. This is especially relevant to the reporting obligations suggested in Section IV of the Discussion Draft focusing on "international tax schemes" (see below).

Alternative ways to understand international tax management

13. As noted in our general comments, BIAC strongly recommends that the OECD considers the many other ways in which countries do and will obtain information on a company's tax arrangements. Tax administrations already have access to a wealth of information that is often not examined. Adding more information without also increasing the capacity of the tax administration to process and use such information will only increase the amount of information reported, without increasing its usefulness.

14. Tax administrations should review annual income tax returns and filings (including the audited accounts of relevant entities prepared under the relevant local Generally Accepted Accounting Principles or International Financial reporting Standards) and Transfer Pricing Documentation. In order to make best use of this information, they should dedicate the necessary staff.

15. An alternative way to obtain insight includes making better use of the list of transactions identified by the Joint International Tax Shelter Information Centre (JITSIC). This list is expanding to include more countries and more potentially aggressive arrangements.

Compliance burden and cost

16. Mandatory Disclosure Regimes are most effective at identifying "mass marketed" or "pre-packaged" schemes. . If the scope of disclosure rules is broadened beyond that, they risk imposing an enormous compliance burden on a huge number of companies that are not engaging in aggressive tax avoidance.

17. The purpose of early identification of new schemes is best served in domestic situations as the tax administrations can respond promptly as information is provided, including by proposing and enacting legislative changes if necessary. In cross-border situations, this may not be possible as the information could be provided to another jurisdiction and the affected jurisdiction might not receive the information promptly. Thus, the principle benefit of a Mandatory Disclosure Regime – i.e. upfront information that facilitates a quick response – will not be realized with respect to cross-border arrangements. BIAC is concerned that the disclosure of international tax schemes will merely be a tool in the hands of the receiving assessing officer, and will only serve their unilateral domestic tax (collection) purposes. We understand that this is not the intention of the proposals.

18. The Discussion Draft proposes that reporting of *"key provisions of foreign law relevant to the elements of the disclosed transaction"* will be required. However, in making this disclosure, taxpayers (and professional advisors) will be entirely dependent on foreign counsel, and will need to rely on advice and information provided by advisors in those countries. These will generally not have, even in the largest firms, the expertise to verify whether that analysis is complete or accurate – in such cases, penalties should not be applied to taxpayers due to understandable errors or omissions in their disclosures.

19. The compliance burden on taxpayers, professional advisors and tax administrations should be proportionate to the expected benefit. In this context, Mandatory Disclosure Regime should identify one jurisdiction for a specific tax arrangement, rather than having a multiple reporting requirement to tax administrations in multiple jurisdictions regarding one tax arrangement.

20. The Discussion Draft recognizes that disclosure is not necessarily intended to expose only 'aggressive avoidance', but any tax arrangement that may have negative tax consequences. We are concerned that this objective is too broad, and as noted in our general comments, would create a disproportionate compliance burden for tax payers and, at the same time, would risk swamping tax administrations with information.

21. BIAC believes that any penalties imposed under a Mandatory Disclosure Regime should be restricted exclusively to tax penalties – whether monetary or non-monetary (such as an extension of statute of limitations). Penalties ought not to include those unrelated to taxes, such as restrictions over the ability to apply for future government tenders.

Risk management by taxpayers

22. The Discussion Draft recognizes that a taxpayer may have a minor interest in a "tax scheme". We believe it is incorrect to assume that all taxpayers s would be sufficiently aware of the material tax or economic consequences for any one of potentially multiple parties to a "scheme". In many instances, the taxpayer will have an obligation to collect information that it does not have and cannot demand. Moreover, the taxpayer may not even be aware of its role, or the materiality of other parts of the "scheme", whether they are related or otherwise.

Promoters

23. The Discussion Draft proposes that a promoter should be required to report a transaction when the transaction is offered to a taxpayer. The recipient of such a proposed tax plan often chooses not to adopt the plan, which may be for many different reasons (often unrelated to the tax plan itself). Disclosure of a scheme should not be required unless and until the plan is adopted. Further, disclosure of tax payers name by a promoter should not be required unless the taxpayer has adopted the plan. Otherwise, connecting a taxpayer to a proposed tax plan may damage their goodwill with its tax administration.

24. A tax advisor who is not a promoter may learn of a tax structure - for example, the advisor may be asked to provide a professional opinion in relation to a transaction. In such a case, the advisor may have information concerning the plan, and, under the OECD's current recommendations,

could have to disclose that to the relevant tax administration(s). The advisor would then be subject to issues of privilege and other relevant ethical rules. In such cases, the advisor's privilege should be respected. If reporting is required, either the promoter or the taxpayer implementing the transaction - and not a secondary advisor - should be the party required to report. Taking this approach would minimize confusion, since the scope of legal privilege differs between countries. The exclusion of such 'secondary advisors' should reduce the applicability of difficult issues concerning privilege; when it will apply and when not.

Penalties

25. Monetary penalties should be related to the 'tax saving' or 'tax liability' and not be a specific sum. OECD best practices should also suggest a clear statute of limitations. Even non-monetary penalties should be related to the actual tax liability or other tax related obligations. That is, an extension (but not unlimited) of a statute of limitations may be appropriate as a penalty/consequence, while precluding a taxpayer from participation in a tender would not.

Need for Disclosures: Hallmarks

26. The use of a "main benefit" test as a threshold for disclosure, particularly if the test is "one of the main benefits" rather than "the main benefit", may result in an undermining of the principle that *"mandatory disclosure rules should be clear and easy to understand."* The main purpose test will result in taxpayer uncertainty and the omission of transactions that governments may want to be made aware of. In addition, taxpayers will be forced to pay for advisory opinions to determine whether the test is satisfied, increasing the difficulty and cost of compliance. Taxpayers may also be subject to penalties when they believed in good faith that disclosure was not required.

'Hypothetical generic hallmarks'

27. BIAC strongly objects to the use of 'hypothetical generic hallmarks'. Taxpayers should be judged by their actions, not by what they might have done. For instance, the reference to 'premium fees' and whether a promoter could have charged a premium fee, but did not, introduces uncertainty and encourages second guessing as to the actual conduct of the parties.

Hallmark loss transactions

28. BIAC cautions against the inclusion of 'acceleration of losses' as a hallmark for a transaction to be disclosed. The draft does not clearly explain when a loss should be considered "accelerated". For example, would the disposition of an asset qualify as acceleration? This test is not consistent with the hallmark for the transfer of losses – either the loss is realized and recognized by the transferor (and perhaps as a result of accelerated depreciation), or the loss carries over to the transferee. Loss trafficking would seem to justify greater concern. Economic losses that have been realized ought generally to be recognized and allowed (subject to any general limitations on the ability to use losses). The ability to claim such losses might be especially significant in a period of economic downturn. Although the Discussion Draft states the disclosure has no impact on whether the loss would be allowed or not, the overall notion is that "schemes" are subject to disclosure and the reported behavior is considered 'suspect'.

International Tax Schemes

29. BIAC has the following comments with respect to the 'International Tax Schemes' proposals:

- A more appropriate approach would be for countries to consider adopting Mandatory Disclosure Regimes in light of this guidance. If countries adopt guidance, then they will define the information they wish to have reported and other conditions around that reporting. If they decide not to require any reporting that decision should also be respected. Thus, only parties immediately involved (based on governing tax law in the relevant jurisdiction) with a transaction should have an obligation to report.

- As noted above, the purpose of early identification of new schemes is best served in domestic situations as the tax administrations can respond promptly as information is provided, including by making legislative changes if necessary.

- Also, as previously stated, Mandatory Disclosure is primarily of benefit to tax administrations when information is provided upfront, therefore permitting an expedited response. BIAC is again concerned that the International Tax Schemes proposals will not provide that benefit, and will only represent a tool for the receiving assessing officer only relevant for unilateral domestic tax purposes.

- BIAC is concerned that although the Discussion Draft acknowledges that domestic taxpayers may have incomplete knowledge of a transaction, international reporting will nevertheless be required. In relation to paragraph 235, we note there will be cases (for example through a bare shareholding) that a parent might not always be able to ensure that relevant data can be gathered to comply with disclosure rules.

- The Discussion Draft does not offer a 'safe harbor' (for instance, for small companies) from reporting obligations.

- The timing requirements for filing any documentation are of particular concern to taxpayers. Many large taxpayers manage thousands of global tax filing obligations throughout the year. These taxpayers already have significant and complex reporting processes in place to ensure proper reporting for recurring obligations. The introduction of reporting obligations inconsistent with these existing timelines will require entirely new and costly reporting processes to be implemented. BIAC strongly recommends that best practices adopt timing requirements consistent with pre-existing reporting regimes (e.g., annual or quarterly tax return filings).

- Reporting of the same transaction may be required in multiple jurisdictions, by taxpayers who are not themselves in any way a party to the cross-border transaction or tax saving (if there is one). In the context of acquisitions, refinancing or restructuring, a large number of group companies may be required to report the same transaction, and each potentially reporting different information at different times regarding the same set of facts. This could substantially increase related reporting costs and effort, with little or no benefit to tax administrations.

- The creation of a reporting obligation by countries that do not have a tax interest in the "international tax scheme" is inappropriate. The Discussion Draft recommends that *"domestic taxpayers should be under an obligation to disclose a cross-border arrangement to the reporting jurisdiction even if they are not a direct party to the cross-border outcome."*[1]

- If the proposed International Tax Scheme disclosure requirements were adopted as they currently stand, detailed guidance would be required for effective implementation by governments, so taxpayers could clearly understand their compliance obligators. Such guidance should clarify taxpayer reporting requirements regarding international tax schemes and how the disclosure rules would work in a multilateral framework. For instance, the 'materiality standard' in the draft is unclear.

Materiality standard

30. The Discussion Draft states that *"an arrangement that incorporates a cross-border outcome should be treated as a reportable scheme if it involves a domestic taxpayer. A domestic taxpayer should be treated as involved in a cross-border arrangement where the arrangement includes a transaction with a domestic taxpayer that has material economic consequences for that taxpayer or material tax consequences for one of the parties to the transaction."*[2]This standard does not offer a clear definition. Even if materiality were clearly defined, the domestic taxpayer would not be in a position to apply the second half of the test, since the information on the tax consequences to the other parties to the transaction may not be in the possession of the domestic taxpayer that has the obligation to report.

31. Example 1[3] "applies" the materiality standard in determining whether reporting is required. It is assumed that a loan from A Co to B Co will have material economic consequences for A Co. There are no facts justifying this assumption. It is possible, and often likely, that a single loan to a related party does not have any material economic consequences to the lender. For example, if A Co has substantial assets and the loan represents a small portion of those assets, and B Co represents low credit risk, it would seem that the loan may not have material economic consequences for A Co. A Co's entire investment in B Co could be immaterial from A Co's point of view, depending on the relative sizes of A Co and B Co and A Co's risk diversification profile.

32. Example 3[4] illustrates both flaws with the materiality test. Paragraph 272 provides that A Co must report as it is a direct party to a cross-border outcome and the transaction has material tax consequences for B Co. Again there are no facts justifying this assumption. A client database may or may not have substantial value, but if the issue is the materiality of the tax benefit then the

[1] Discussion Draft, paragraph 241.
[2] Discussion Draft paragraph 243
[3] Discussion Draft paragraphs 257 through 261.
[4] Discussion Draft paragraphs 270 through 274.

outcome should depend on the relative value of that benefit to the tax liability of B Co. If A Co does not have information concerning B Co's overall tax situation how will A Co apply this test?

33. The Discussion Draft does not deal with reporting between countries. Reporting this information to the country that is not affected by the cross-border arrangement will undermine the principle benefits of a Mandatory Disclosure Regime. The transfer of disclosed information to the jurisdiction that may have a taxation interest in the transaction would likely not reach the other country quickly as the information would likely need to go through a process of exchange of information under a treaty. In addition, the disclosed information may be incomplete and difficult to understand.

34. In particular, paragraph 230 raises the issue of reporting with respect to cross-border tax planning "schemes" regarding 'acquisitions, refinancing or restructuring'. The OECD's guidance with respect to the Transfer Pricing master file and local file (BEPS Action 13) will already require reporting on these transactions both globally and locally if the transaction affects the local country business. Additional reporting – especially before the OECD's revised Transfer Pricing Documentation guidelines have been evaluated – will likely be duplicative and will increase taxpayers' costs significantly. Disproportionate increases in administrative burden and compliance costs are especially likely in this area due to the modular design of the Mandatory Disclosure Regime. Such a design framework will result in different requirements across jurisdictions as countries will pick and choose from the modules that serve their national interests. This runs counter to the design principles under Action 13, where the OECD attempted to achieve consistent reporting, partly to limit the cost of compliance.