

Tax Transparency and BEPS

Owens, Jeffrey

Published in:
Journal of Tax Administration

Published: 01/01/2015

Document Version
Publisher's PDF, also known as Version of record

[Link to publication](#)

Citation for published version (APA):
Owens, J. (2015). Tax Transparency and BEPS. *Journal of Tax Administration*, 1(2), 1-10.

Tax Transparency and BEPS

Jeffrey Owens¹

The following is a modified version of a keynote speech presented by Professor Owens at the Tax Administration Research Centre Workshop, held at the University of Exeter, 21-22 April 2015.

We are moving into a new era where the traditional relationships between tax administrations, tax advisors and companies are changing: moving away from confrontation to cooperation. At the same time, there remains some hope that a new consensus will emerge from the OECD's Base Erosion and Profit Shifting (BEPS) project on a revision to the international rules of the tax game. This paper explores these issues.

Cooperative Compliance

The concept of cooperative compliance was initially launched in 2008, with a lot of help from Her Majesty's Revenue and Customs (HMRC), but it was referred to by the term, "enhanced relationship". It would not have been my choice of name for this concept. The Dutch and the Koreans refer to it as "horizontal monitoring". I don't like that either. That gives the suggestion that one party lies down and the other party walks over you, which is not what cooperative compliance is about. So today we have the term, "cooperative compliance". Whilst it is better, I suspect it will evolve. The concept is all about a change in the dynamics of the relationship between these three key players in the tax world. Moving from a relationship that is characterized by reference only to the legal requirements to one where multinational enterprises (MNEs) comply with the spirit of the law. You can argue what that means in practice, but it isn't that difficult to determine. You move from a relationship that is characterized just by reference to the legal obligations and with limited disclosure, with no signals of uncertainty. In other words, the taxpayer is not going to ask HMRC, "you know, we're not quite sure this scheme's going to work. What do you think"? That seems kind of a strange thing to ask, but if you have a dialogue it can be done. You try to move away from that non-constructive dialogue to a relationship where you have mutual trust; a relationship where the taxpayer is prepared to disclose what they're doing, it's prepared to help the tax administration to understand their business model, why they're changing it, why they're undertaking business restructuring. At the same time, the tax administration is open with the taxpayer. And that has to start at the level of policy formulation, where you have a dialogue with business, you tell them what you're thinking of; at the level of implementation of the policy decisions that you make; and in monitoring to ensure that the laws are actually implemented in a consistent way. It sounds simple but it's not easy to achieve.

What does it require if we're going to move in that direction? The first thing is building up trust and, as we all know, it takes a long time to build up trust,

¹ Professor Jeffrey Owens is Director of the Global Tax Policy Centre at the Institute for Austrian and International Law, WU Vienna University of Economics and Business. He was formerly Director of the Centre for Tax Policy and Administration at the OECD.

particularly in the tax area. On the other hand, you can lose trust very quickly. And if you're going to get this change in culture – because we are talking about a culture change here, you may have to also have legislative changes as well to make it work. But essentially it's cultural change, which has to start at the top. The tax Commissioner and his deputies must firmly commit to the programme. You also have to have the CEO and the board committed. No MNE should go into a cooperative compliance programme unless the board has had a discussion. "Is this something we want to do, and do enthusiastically?" But even that is not enough. It then has to percolate down to the operational level, and that has been a problem, and it's where the cultural change comes in. Because if the auditors on the ground don't understand that there has been a change in the climate, it's not going to work. The same applies to MNEs. If the people that design the tax planning schemes, including the advisors, do not realise that things have changed, then they just continue in their old ways, not being afraid to cross the red line of acceptability and so cooperative compliance is not going to work. In practice, even for countries like the Netherlands or the UK, it takes a long time for the change to percolate down. And that's where it really is a cultural change; a generational change. So be patient. It will take time, but it is worthwhile persevering.

The other thing cooperative compliance requires is that tax administrations have commercial awareness: that they understand how business operates; and that business in turn understands what drives the tax administration. One thing that can help here is that many countries are moving to a situation where there's much more of an exchange of personnel between the business sector and the government sector. I don't think we want to get to the US situation, where you design schemes; then two years later you are in the private sector and you exploit those same schemes. That's perhaps not where you want to go. But I think having more movement of staff between the private sector and the tax administration is a positive thing. There are some countries where that is just not accepted. In France, for example – if you are a senior tax official and you leave the tax administration, it's a one-way exit; you can't come back. That's the wrong approach, in my view anyway.

A further issue that has to be addressed in the cooperative compliance space is confidentiality. Because when you provide information in the context of the cooperative compliance programme, you can't take it back; you can't suddenly forget it. So you have to be sure that the tax administration will not exploit it. And also, on confidentiality, there is the question of how widely information should be shared. Some MNEs may be happy that, say, the UK gives information they get under the cooperative compliance programme to the US; they may be far less happy if it ends up in Sudan.

Where does this programme of cooperative compliance currently stand? I would say that there are probably less than 8 countries that have actually implemented true cooperative compliance programmes. There are many other countries that say, "we have it", but it is more rhetoric than reality. They think, "Ah, now we have an occasional lunch with a tax director, this is cooperative compliance". That's not the way it works. Genuine cooperative compliance requires a fundamental change in the way the tax administration works, and it requires

legislative change, it requires cultural change, it requires a change in the way information is handled. This is not something that can be put in place overnight. It takes a long time – and it does require resources; significant resources of high-level staff at the beginning – but once you have it in, it pays for itself.

Where are we going today? It's difficult. In some ways, cooperative compliance is suffering from collateral damage from the BEPS project. There are very few Commissioners that are going to be prepared to stand up and say, "I love the taxpayer. Let's sit down and have a nice conversation." And there are very few companies that are prepared to take the risk of being very open in the current environment. So we need to know how to kick start this process. Because I believe, quite strongly, that many of the issues in the Base Erosion and Profit Shifting project are going to be much easier to solve if we have this type of dialogue. And I think this is not just the case for the OECD countries; it is also the case for developing countries. So I hope we can move forward. The WU Global Tax Policy Center at the Institute for Austrian and International Tax Law (part of WU Vienna University of Economics and Business) has just launched a project on cooperative compliance with support from the Tax Administration Research Centre (TARC) at the University of Exeter. We aim to get two or three countries in Africa and two or three multinationals to volunteer to go into this programme. I did this successfully in Russia. At the end of two years' negotiation, we managed to get in place a cooperative compliance programme. There are five multinationals in the programme and it seems to be working. If you can do it in Russia, you can probably do it anywhere.

BEPS

And now to BEPS; you can't go to any tax conference these days without using the word, "BEPS". I'm sure you are all familiar with BEPS, so I'll just give you some high-level comments.

Launched in 2013 by the OECD, it is the biggest tax game in town. It poses an enormous reputational risk for the OECD; if they don't succeed in this, they're going to have a problem moving forward on the broader tax agenda. If you want to see the first BEPS report, go back to the 1998 report of the OECD on Harmful Tax Competition. Almost everything that's in the BEPS project is there. And almost everything that is being worked on in BEPS was being worked on by the OECD over the last 20 years: so what's the difference? There are three distinguishing factors. First, BEPS is a package. That was not traditionally the way the OECD worked. You looked at a particular issue, isolated it, you had a long period of technical discussions, you came up with proposals and within five years you had a couple of recommendations. That's not the way it is happening today. All these issues are part of a package. That has its advantages and disadvantages. The advantages: as a package, you can get trade-offs. The disadvantages are that you don't always get the right technical solutions. The second distinguishing feature of the BEPS project is the political support. This is very much a project that is a top-down rather than bottom-up project. Thirdly, the timelines: basically the OECD was given until November 2015 to deliver on the 15 Action points. That is a very tight deadline. What was pushing it? A lot of people say it was the global financial crisis, the need for money. Obviously, those

are important drivers. But I think there were also at least two or three other drivers that were perhaps equally important. One was this feeling that, if we're going to build up support for exiting from the crisis from citizens – citizens who are seeing their benefits cut, and their taxes increase – you must be able to show them that everybody is paying their fair share of tax. It is an important political driver. Another driver was the feeling that, for companies that were prepared to push the envelope that would give them a competitive advantage. Our American friends are very good at pushing the envelope. It's no coincidence that most large US multinationals have effective tax ratios which are significantly lower than European multinationals. The US system was set up in such a way that some, not all, of its MNE do get a big competitive advantage, despite its high nominal rate of corporate income tax.

So what is the BEPS project trying to achieve? There are three broad objectives that are set for BEPS. One is to get a fairer sharing of the tax base between countries. The second is the counteraction of non-compliance, particularly by means of MNEs using tax havens. And the third is to update the rules of the game that the OECD has been working on for the last 50 years. The 15 Action points can be conveniently grouped into three groupings. There are those that are primarily concerned with transparency: the disclosure provisions, the country-by-country reporting, even the master file of transfer pricing. There are those that look at substance: this whole idea that, if a tax scheme doesn't have substance behind it, then somewhere something's gone wrong. And substance is not having one highly-paid lawyer with a lovely sun tan in a Caribbean island, sitting behind 600 brass plates. So there's a whole debate going on of what do we mean by substance? And that's not going to be easy – as you can see from the CFC discussion draft. And then, the third theme that runs through the whole programme is coherence. We need a greater coherence in the way that different parts of the international tax system interact.

In terms of what has been achieved so far, my ex-colleagues in the OECD, have managed to deliver on time high quality technical products. Seven of the Action plans resulted in recommendations to the G20 heads of government when they met in Brisbane in 2014, although many were what I call, "qualified". There was no clear consensus saying "this is what must be done"; it was more analysis and then options about each issue. The remaining eight Action points are to be delivered by November 2015. This is the point where the rubber hits the road, because up until now BEPS has been about analysing problems, putting forward options; now they're going to have to say "hey, this is what you heads of government have to agree to do". And that's where it gets difficult. And it partly gets difficult because different countries have gone into the project with different objectives. The BRICS were entering the project primarily because they saw it as an opportunity for revising the international rules of the game, particularly the division of tax between source and residence countries. The US and some other big countries went into the project primarily because they were tired with the way their multinationals were using tax havens to minimize their tax burden. Countries like France and Italy were more concerned with digitalization. So lots of different objectives, which meant it was going to be difficult to get a consensus on the 15 Action points.

BEPS is not going to finish in November 2015 at the Turkish summit. This is just going to be another staging point in the process. After November 2015, there'll be much more emphasis on implementation, and much more emphasis on the tax administration aspect, which brings it back to the type of work that is being done at TARC. This is a project that is worthwhile looking at on a longer-term basis. The other comment is if governments were primarily interested in more money, they've chosen the wrong tax. In a typical OECD country, the corporate income tax yield is about eight per cent of total tax revenue, with about 70 per cent of the revenue coming from multinationals and of that 70 per cent, maybe a third potentially related to Base Erosion and Profit Shifting. So even if BEPS is fully successful, maybe it's a one or two per cent increase in overall taxes. Now look at VAT: 20 per cent; tax gap 15 per cent. So maybe what we need is a BEPS VAT programme the next time round.

In developing countries, the reliance on corporate income taxes tends to be much higher; 18 to 25 per cent. But a lot of the issues that are coming out of the BEPS project may not be a priority for developing countries. For developing countries, the priority has to be improving the capacity of tax administrations. If you do not have a good tax administration, there is little you can do about BEPS.

Exchange of Information

The other change that has occurred is the whole question of exchange of information. And it's rare in the tax world that you have a revolution, but I think this is one example where there is a revolution. I spent 20 years of my life trying to get countries to agree to give up their bank secrecy. Look now at the change. Ministers in Switzerland saying, "we will now move into the automatic exchange of information scheme". I haven't heard a finance minister stand up recently and say, "we defend bank secrecy as the barrier to effective exchange of information". And that is one of the legacies that former UK Prime Minister Gordon Brown can be proud of, because without him and his pushing at the April 2009 G20 Summit, we wouldn't be where we are. So we have seen a revolution in terms of exchange of information (EOI) on request. And keep in mind that for tax administration, information is the life blood. Deny a tax administration access to information, and it can't operate effectively. We have now got that in place – and it's beginning to work.

But what is interesting from my perspective is that, despite not having completed the EOI on request process, the G20 have now said the new standard is going to be automatic exchange of information. You want to have all forms of exchange of information on the table: spontaneous, automatic and on request. It is much more challenging, the automatic exchange. And if you don't believe that, ask the EU countries how long it took them to implement the savings directive. Ireland, a pretty sophisticated tax administration: five years. It's a big investment for a tax administration. The EU now said that once all this is operational, the savings directive will disappear. Because that's what you want; because you need to work towards global standards; because without the global standards, you can't take advantage of the technology that's coming in place to minimize the compliance costs to the taxpayers, and to maximize the usefulness of the information for tax administrations. So, there's a big challenge there.

Once we've gone through this process of increased cooperation between tax administrations on the assessment side, the elephant in the room then is what do we do about collection? Because very few countries are prepared to help other countries claim tax. And the amount of tax debt: at one point I think the OECD estimated it at somewhere at 450-500 billion dollars' worth of uncollected tax. And that's just in the OECD area. You extrapolate that to developing countries, it's probably a multiple of that figure. So it's great having assistance in assessment, but can we move to the next stage of assistance in collection? And there is now a provision, Article 27 in the OECD model for that. But let's put it this way, there's not much enthusiasm on the part of countries to move in that direction, because they are still in the old world of national sovereignty, and that's something I will come to.

Country by country reporting and other reports

The other issue that is a BEPS-related issue but I wanted to pick out is the question of country-by-country reporting. Again, that was a concept that we launched at the OECD in 2010. We did a feasibility report. It was a great report. It began by analysing what the issue was. It then looked at what were the options and what were the consequences. And it made recommendations. It was so good a report that the OECD refused to publish it. But we managed to get Mike Devereux, Director of the Oxford Centre for Business Taxation to publish it, without any reference to the OECD. That really kicked the debate off, and it was part of a response to the tax campaigning non-government organisations (NGOs). Eventually it came back on the agenda of the G20 and now it's a reality. A lot of companies refuse to recognize that, but I say to them, "look you have to start preparing for country-by-country reporting". It means that multinationals will have to provide a lot more information to the tax administrations in which they operate, and it's got to be done.

This was the most contested part of the BEPS project. There were a lot of multinationals that really didn't want it. Why didn't they want to do this? They said, "we don't have the information". It is a little bit difficult building up the picture for the legal entities, but it's not impossible. There is a compliance cost, but that's inevitable when you change some of the rules. The one area where I do share some of their concerns is on the confidentiality issues, although a lot of this information I don't think is commercially sensitive. But I can see that they are concerned about the potential for the information to be misused; there is also concern that this is a first step away from the arms' length principle towards global formulary re-apportionment. The OECD has tried to address this by saying the information would only be given to tax administrations. Let's get real. When the review is undertaken in 2020, what's the first thing they're going to decide? The information has to go public. So I say to multinationals, "if you're preparing this information, prepare it on the basis that everything you put there is going to get in the public domain." And maybe that's not a bad thing. If we want sensible debate on tax policy, the citizens need information. And yes, it's complicated, but you need to then explain it; that's the role of politicians and it's the role of tax advisors as well. It's going to be an interesting debate.

There is a risk that the information will be misused, particularly by non-OECD countries, to adopt the more aggressive approach; one that is more based on profit-split, more based perhaps on some sort of transitional pre-decided formulary re-apportionment as well. But in many ways, I think, that's a healthy debate to have. It does mean that you have information in the public domain, and that is only to the good. Better transparency is the first step towards getting that trust into the system.

The one thing that may be a mistake is that the information on the country-by-country reporting will be exchanged via the treaty network. It's cumbersome; it's not in real time; and it's going to effectively exclude many developing countries. There is another way it can be done, and that is to put the information into the cloud. Registered multinationals and registered tax authorities would have access to the cloud. Are there more confidentiality risks in that? No. confidentiality issues remain the same. What new technology people tell me is actually it's probably *more* secure. We had a meeting in Vienna in April 2015 with a mix of service providers, businesses, tax administrations, academics and government – and that was the conclusion they came to. Or as somebody suggested, why do we need to have all of these different pipelines? Why can't tax administrations just have direct access into the accounts of multinationals? Revolutionary idea! Think how easy that would be. And who owns the data of the multinationals? Such an approach would minimize compliance costs.

Now let's go to the Master File. It sounds a very Orwellian concept, the Master File, but it is actually quite a useful concept because it really sets out what type of information should be provided by multinationals to tax administrations. This information will be provided by subsidiaries to the tax administrations within which they operate. There's not much new that's here, but I think what is interesting is it's in a standard format. The idea was to combine country-by-country reporting with Master File. That was split. Why? Because of the concerns about formulary re-apportionment. So if you put all this together: a combination of country-by-country reporting, the Master Files, Exchange of Information – the tax administrations are going to have much more information than in the past for transfer pricing and that can only be a force for good.

Impact for Tax Administrations

Technology: I won't spend very much time on this, but if you want to be serious about a tax administration reform, you need to get into the technology. Commissioners are scared when it comes to technology, because they know it costs a lot of money and, once you make the decision and invest the funds, you are blocked. The US Internal Revenue Service has one of the poorest technology systems in the world and it is very hard to change because of the legacy issues there are. So you've got to get it right. And every day you get proposals coming across the Commissioner's desk: "why don't you do this?" and "why don't you do that?" How do they choose? Some administrations have begun appointing data analyst advisors; not tax people. But I think there is an enormous potential for technology to change the way that tax administrations work. And as I said, if you look at putting country-by-country reporting in the cloud, you've got a really effective tool. And it is not just using technology to get the information, it's using

technology to analyse the information – big data. Because all of that – the combination of better access to information, a better capacity to analyse the information, using big data – what do you get? Better risk assessment and better risk management. So you move away from a blanket audit approach to one that is much more selective. Developing countries can benefit significantly from such an approach.

How do governments and business take advantage of this more open, more transparent environment? To me, the key is for government to think very carefully how they exploit all the information. For tax administrations and for business the key message is the old days of deals being done in the back room have gone. If you're a big multinational, you have to now see that any information that you give to one tax administration is going to get around the world. So the days when you could play off the UK against the US by giving one set of information to one country and another to another have gone. And the implication is that multinationals are going to have to have a much more globally consistent approach to information sharing and compliance. And some MNEs are appointing a global tax policy officer – not a bean counter, but somebody that actually takes a global view: “what are we doing in terms of our approach to tax planning on a global basis?” So, lots of interesting things happening there.

Let's move to ask what sort of vision we could form in terms of where tax administrations will be by 2030. We will continue to see a tendency to strip out the policy function from tax administrations, so that they do focus on implementation, although the borderline between tax administration and policy is fluid. We will see tax administrations that are leaner, meaner and smaller: and yet, they will be asked to do more things – more things that are not linked with revenue collection. The way they'll resolve this conflict is by using technology. And perhaps that's not a bad thing, the fact that there is some shrinking of some of the bigger tax administrations. So, we will see a lot of the assessment functions outsourced. In other words, you will be using third-party intermediaries not just to collect the tax, but also to assess the tax. Russia is quite a good example of that. You'll see more use of withholding taxes. We will see more countries moving into the cooperative compliance space, because that is the answer to a lot of the issues that we face today. There'll be more emphasis on protection rather than detection; or, put another way, a lot of the issues that arise in a debate between the tax administration and a company, there'll be a real effort made to resolve these before you get into the audit – the compliance assurance programme (CAP) in the US, for example. And that has advantages for tax administrations and for the taxpayer. We'll continue to see the spread of special units. Most countries now have large business units; many – not enough in my view- have high net wealth individuals, while some countries have SME units. And of course, countries that are rich in natural resources have units that specialize just in the extractive industries. That's a good thing because it builds up expertise of the tax administration.

We will see a more sophisticated approach to risk management. 25 or 30 years ago, the attitude of most tax administrations was to audit. (50 per cent of enterprises was not uncommon). The typical audit rate in OECD countries today is less than two per cent. You say, “how can we do that”? You can do it if you get

good risk management. And we need to get the developing countries into this mentality, because they waste a lot of resources at the moment.

Another point is that we see a new emphasis on the work being done by behavioural scientists, tax psychologists, tax sociologist on how to influence attitudes towards compliance. And I am glad to see that's something that you're working on here at TARC. I also think that, with all the information technology that we have and all the additional information that tax administrations will get, particularly from third parties, that we'll see a massive move towards pre-populated tax returns. Ten years ago it was only the Nordics that had this in place; today there are a few more countries, but there are still too many OECD countries that don't – the US, for example. I think one of the reasons in the US is that you have 460,000 tax assessors that will basically lose their jobs. That's a pretty powerful lobby. But we *will* get there so that paying your tax becomes almost a pleasure! You get your tax return from the tax administration, it is all completed, you look through it, the information is right, you then tick it and automatically the amount is deducted from your bank account. It works in Norway: 90 per cent of the returns that are dealt with in this way are correct, and 90 per cent end up by paying the tax automatically. It is a painless system. Now, if you believe in the small government, you may not like that. As Milton Friedman once said to me, "I like to make tax as painful as possible." Not sure it's the right way to approach it, but that's the US. We will see a greater integration of audit of VAT and of corporate income taxes. Some countries have got there already, like Australia; but many countries still have separate reporting, even when you have large business units. But if you think about it, the information you need for a VAT audit is extremely similar to the information that you need for a corporate tax audit.

You will also see the move from bilateral to multilateral approaches. You'll see this in audits already. You've got a number of countries undertaking multilateral simultaneous audits, multilateral joint audits and I hope, we will see the same in advance pricing agreements (APAs). I've never liked unilateral APAs. If you can't tell your treaty partner what you've done in the APA, there is something wrong with it. So I like the idea that more countries are moving to the bilateral APAs; the next move is multilateral. There are one of two companies and one or two countries that have begun that process. It's not easy, but it can be done, and it is a more effective way, both from the perspective of the tax administrator and the perspective of the company. This move to multilateralism is spear headed by the OECD multilateral convention on administrative assistance in tax matters. It has something like 80+ signatures now. It is a massive change.

I also hope we will see a move towards tax arbitration. I do not understand why tax people are so against – well, I *do* – mandatory arbitration. Why is it that the investment people can go in that direction? Why do the financial people go in that direction? Free Trade Agreements including the proposal between Europe and US have dispute resolution mechanisms. The WTO has done it. And we the tax people, it's not our culture. So what do you get? Unresolved tax disputes. The UK/US Glaxo Smith case that took fifteen years to get a solution. In a post-BEPS environment we will need a guaranteed outcome. But in mutual agreement procedures, there is no obligation on the tax administration for a final agreement; it's just to try their best endeavour. That's not enough today. And that's why, at

Vienna, one of the things I've launched is a project on the tax disputes. The report the OECD put out in their Discussion Draft on Action 14 threw down the glove. It was giving up too easily under pressure from the BRICS. We need to move forward on that since BEPS, at least in the transitional period, is going to generate a tsunami of tax disputes.

So overall, what are we going to see in ten years' time? We will see tax administrations that are smaller; that are much more comfortable using new technologies to deliver service, to deliver enforcement; that interact with the treaty partners much more effectively; that interact with other government law enforcement agencies – financial intelligence units, justice departments – to counter all forms of illicit activities; and that have much greater commercial awareness of what's happening in the private sector. You will find that multinationals will, slowly, perhaps painfully, get used to operating in a much more transparent environment. What I predict is that in ten years' time, when we look back at this debate we will say: "Country-by-Country, what was all the fuss about? What was it all about?" Information sharing.