GLOBAL TRANSFER PRICING & DISPUTE RESOLUTION SERVICES

THE OECD'S BASE EROSION AND PROFIT SHIFTING ACTION PLAN

NEWSFLASH – TRANSFER PRICING PRACTICES TARGETED

The G20 Finance Ministers have endorsed the Base Erosion and Profit Shifting ("BEPS") Action Plan released by the Organisation for Economic Co-operation and Development ("OECD") on July 19, 2013. The Action Plan was drafted to address growing critiques that large-scale multinationals (such as Google, Starbucks, Amazon, Apple and others) were utilizing existing tax legislation to avoid paying corporate income taxes. The concern amongst tax jurisdictions is that tax laws developed in the twentieth century do not adequately address the global and digital aspects that characterize businesses operating today. The Action Plan is intended to "provide countries with domestic and international instruments that will better align rights to tax with economic activity."[1] The OECD aims to develop a new set of international standards to "ensure the coherence of corporate income taxation at the international level."

The BEPS Action Plan consists of 15 suggested international tax reforms to address "gaps" in international tax and transfer pricing rules that the OECD says allow some multinational taxpayers to "separate" income from economic activities that produce it and "artificially shift it into low-tax environments."[2]

Specific Actions on Transfer Pricing

Transfer pricing is a targeted topic of the Action Plan, with four of the 15 suggested actions directed at revising existing transfer pricing rules. The Action Plan argues that international transfer pricing rules should emphasize "valuation creation" rather than an arm's length standard, and focus on "intangibles, risks, capital and other high-risk transactions" utilized "to shift profits."[3]

While all of the 15 actions address related party transactions that cross borders, Actions 8, 9 and 10 are to "assure that transfer pricing outcomes are in line with value creation"[4] and Action 13 addresses transfer pricing documentation.

Specifically:

Action 8 – Intangibles: The task force should develop rules to prevent BEPS via the shifting of intangibles amongst group members. This includes:

- adopting a broad and clearly delineated definition of intangibles
- ensuring that profits associated with the transfer and use of intangibles are appropriately allocated in accordance with value creation
- developing transfer pricing rules or special measures for transfers of hard-to-value intangibles
- updating the guidance on cost contribution arrangements

Action 9 – Risks and Capital: The task force should develop rules to prevent profit shifting when group members transfer risks among themselves or allocate 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."

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[1] OECD (2013), *Action Plan on Base Erosion and Profit Shifting*, OECD Publishing. p. 11

[2] Ibid. p. 13

[3] Ibid. p. 14

[4] Ibid. p. 20

Action 10 – High-Risk Transactions: The task force should develop rules to prevent profit shifting when related parties engage "in transactions which would not, or would only very rarely, occur between third parties." The action plan states that this will involve adopting "transfer pricing rules or special measures" to:

- clarify the circumstances under which transactions can be recharacterized;
- clarify the application of transfer pricing methods — in particular, profit splits — in the context of global value chains; and
- protect against common types of base eroding payments, such as management fees and head office expenses.

Action 13 – Transfer Pricing Documentation: The task force should develop rules for transfer pricing documentation to "enhance transparency for tax administration, taking into consideration the compliance costs for business." This action also includes working to improve the effectiveness of the Mutual Agreement Procedure ("MAP") amongst taxation authorities.

Implications for Taxpayers

The rules will require that multinationals provide "relevant governments with needed information on their global allocation of the income, economic activity and taxes paid among countries according to a common template." Implementing a common template amongst twenty different countries could be challenging, to say the least.

The impact on Canadian taxpayers will become apparent as the plan is implemented over the next two years. The OECD has noted that some of the actions taken likely will result in revisions to the OECD Model Tax Convention, including changes to both the Permanent Establishment definition and transfer pricing provisions, as well as changes to combat treaty abuse.

To fully understand the details of the BEPS Action Plan and its implications for businesses in Canada, please speak to your BDO representative, or contact a member of BDO's transfer pricing team.

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OUR FIRM'S TRANSFER PRICING TEAM

Please see the attached page highlighting the members of BDO Canada's team of transfer pricing professionals.

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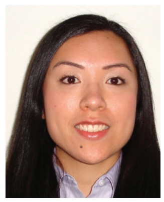

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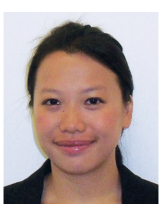

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