THE POWER OF BEING UNDERSTOOD

AUDIT | TAX | CONSULTING

RSM

What to do when you are drowning in tax acronyms

(a brief history of international tax reform)

Thought Paper

This thought paper provides an understanding of the international tax reform process, its related acronyms, and the implications for your tax management.

www.rsm.id

A brief history of international tax reform

If you are part of an international group and responsible for tax matters then you are aware that the international tax environment is undergoing rapid change. Since 2013 the OECD and G20 have been working on actions intended to reform international tax. In some ways this is a misnomer – there is no global tax law or World Tax Office and therefore "international tax" ultimately becomes "domestic tax" because the relevant entity is assessed in one or more jurisdictions under domestic legislation. The international perspective arises from the implications of tax legislation in each of your countries of operation to your international transactions, supplemented by the overriding operation of bilateral double tax agreements.

This thought paper provides an understanding of the international tax reform process, its related acronyms, and the implications for your tax management.

BEPS – Base Erosion & Profit Shifting, and the G20/OECD BEPS Project

BEPS refers to tax planning strategies that exploit the gaps and mismatches in tax treaties and domestic tax rules to artificially shift profits to low or no-tax locations where there is little or no economic activity. As a consequence there might be little or no overall corporate tax paid on the shifted profits. In most cases these strategies are legal tax minimization rather than evasion of tax obligations. Of particular concern is the digital economy whose structure (i.e. replicating intellectual property for value creation) and rapid development is poorly addressed by most countries tax regimes.

The OECD – Organization for Economic Co-operation and Development (which is generally considered to be the club of the rich/developed countries) had previously identified BEPS as a significant issue and was working its way through various identified issues in a methodical manner. These activities appeared to have been turbo-charged by the impact of the global financial crisis on government budgets plus the involvement of the G20, which groups the 20 largest economies (and has a broader developing and developed country membership compared to the OECD).

This resulted in the G20 and the OECD working together on an equal footing and the announcement and endorsement by the G20 in July, 2013 of the BEPS Action Plan. The BEPS Action Plan identified the following areas for review:

Action 1:	Addressing the Tax Challenges of the Digital Economy
Action 2:	Neutralizing the Effects of Hybrid Mismatch Arrangements
Action 3:	Designing Effective Controlled Foreign Company Rules
Action 4:	Limiting Base Erosion Involving Interest Deductions and Other Financial Payments
Action 5:	Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance
Action 6:	Preventing the Granting of Treaty Benefits in Inappropriate Circumstances
Action 7:	Preventing the Artificial Avoidance of Permanent Establishment Status
Actions 8–10:	Aligning Transfer Pricing Outcomes with Value Creation (TP aspects of intangibles, TP risk and capital, TP risk/high-risk transactions)
Action 11:	Measuring and Monitoring BEPS
Action 12:	Mandatory Disclosure Rules
Action 13:	Guidance on Transfer Pricing Documentation and Country-by-Country Reporting
Action 14:	Making Dispute Resolution Mechanisms More Effective
Action 15:	Developing a Multilateral Instrument to Modify Bilateral Tax Treaties

At the time of the initial announcement, the timetable for review, analysis and preparation of reports on these 15 action items was considered ambitious. There were also questions as to whether all the countries were equally committed to completion of the work let alone implementation of the results.

All reports, however, were completed and issued on time in 2015.

For reasons of time and space an analysis of the details of the reports of the various action items will be left for future articles. In general, though, the reports provide a mix of recommendations, minimum standards and updated guidance. Although the BEPS Action Reports are not law and it remains for each country that was part of the BEPS project to implement the recommendations into their domestic law, it should be noted that the proposed changes to the OECD's Model Tax Convention (MTC) and the Transfer Pricing Guidelines (TPG) will have implications for renegotiation of tax treaties and revision of domestic transfer pricing rules and regulations when countries sign the multilateral instrument (MLI) that is recommended under Action 15.

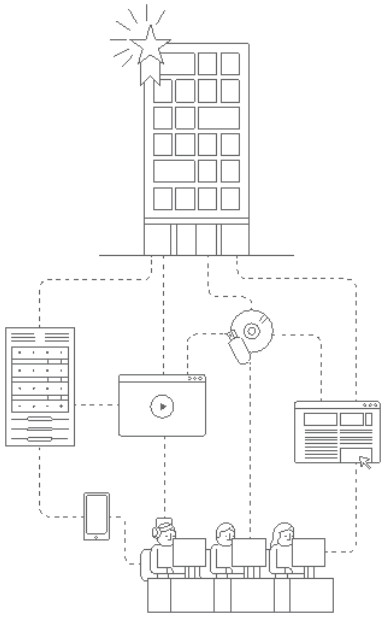
Furthermore the Action Reports are not the "final answer". The OECD continues to work on areas of concerns, especially in relation to harmful tax practices, treaty abuse and transfer-pricing regarding financial transactions and the use of profit splits. Therefore we can expect more announcements and developments in the future.

Prior to the release of the BEPS Action Reports there were indications that some countries were "going it alone" in certain areas rather than acting together. For example the United Kingdom has enacted the so-called Google Tax (technically, the Diverted Profits Tax – DPT), and Australia has followed suit, by introducing its own Google Tax (technically, the Multinational Anti-Avoidance Law – MAAL). In both cases, these new laws operate unilaterally against specific perceived MNC tax avoidance, viz artificial avoidance of permanent establishment (PE) status. Similar pressures exist in many countries to take action.

Against this back drop of unilateral action, several important multilateral steps have been taken that have significance for MNCs.

the BEPS Action Reports are not law and it remains for each country that was part of the BEPS project to implement the recommendations into their domestic law.

AEOI – Automatic Exchange of Information



Automatic exchange of information is the systematic and periodic transmission of tax information by source countries to the taxpayer's residence country concerning various categories of income, such as dividends, interest, gross proceeds of financial transactions, royalties, salaries, and pensions.

This compares to existing exchanges of information in response to specific requests by one jurisdiction to another.

Strictly the AEOI process is not a consequence of the BEPS Project but is driven by the view of revenue authorities that the existing reactive specific request system facilitates widespread non-disclosure by taxpayers – and a more comprehensive system was required.

That is, the objective of AEOI is to shine the light on accounts being used to hide assets (and income) that might be taxable in the holder's place of tax residence.

The **Convention on Mutual Administrative Assistance** in Tax Matters and Article 26 of the OECD Model Tax Convention provide a basis for all forms of information exchange.

Following development of a standard for exchange of financial account information under the USA's FATCA (Foreign Account Tax Compliance Act) legislation in 2013 the Finance Ministers of France, Germany, Italy, Spain and the UK announced their intention to exchange FATCA-type information amongst themselves in addition to exchanging information with the United States. The commitment to automatic exchange as a standard was further widened when, in June, 2013 the G8 Leaders, and in September, 2013 the G20 Leaders at their summit, endorsed the OECD's proposal to establish a global model for information exchange, inviting the OECD to work together with the G20 to develop a standard. This saw creation of the standard and approval of the Standard for Automatic Exchange of Financial Information in Tax Matters by the OECD Council on 15 July 2014. The full Standard (**Standard for the Automatic Exchange of Financial Account information in Tax Matters**, or more succinctly, the **CRS – Common Reporting Standard**) was endorsed by the G20 Finance Ministers at their meeting in Cairns in September 2014, as well as by G20 Leaders at their Summit in Brisbane in November 2014.

Since then the European Union has agreed to implement the new Standard in the EU and the Global Forum on Transparency and Exchange of Information for Tax Purposes (involving more than 120 jurisdictions) has endorsed the Standard, creating a commitment process to enable its members to publicly commit to a timetable to implement the new Standard.

96 jurisdictions have since made that commitment – some to commence the automatic exchange of information by September, 2017 ("the early adopters") and others to commence by September, 2018.

The commitment process, however, is a political one – similar to commitments made to reduce climate changing emissions. Therefore what are more significant are the actions of various jurisdictions to implement their commitment. That is in general countries need to:

- Translate reporting and due diligence requirements into domestic law (e.g. so that relevant institutions are required and have the authority to obtain data) – these might already exist because of FATCA obligations or other legislated requirements (e.g. re: KYC for anti-money laundering)
- Select the legal basis for the exchange of information (e.g. on a bilateral basis under a tax treaty or on a multilateral basis via the **Convention on Mutual Administrative Assistance in Tax Matters**)
- Set up administration and IT infrastructure to collect and exchange information
- Protect confidentiality and data safeguards

Convention on Mutual Administrative Assistance in Tax Matters

94 countries (including Indonesia and Singapore) have signed the Convention since its inception in 1988.

The Convention is not specific to AEOI matters. For example it includes provisions relating to assistance to enforce tax debts, and joint examinations of taxpayers resident in member countries.

Article 6 of the Convention provides that countries may automatically exchange information based on their mutual agreement.

Article 6 is therefore the foundation for the AEOI process and, arguably, should see all 94 signatories sign the **Multilateral Competent Authority Agreement re AEOI** (unless they wish to proceed bilaterally).

MCAA – Multilateral Competent Authority Agreement re AEOI

The MCAA (AEOI) is an instrument for implementing the AEOI and eliminates the need for the relevant countries to sign specific bilateral agreements. It is still necessary, however, for countries to initiate the exchange of information by filing notifications to the relevant country under Section 7 of the MCAA (AEOI).

On 29 October, 2014, 51 countries signed the Multilateral Competent Authority Agreement with an additional 29 countries signing until 16 February, 2016, bringing the total to 80 countries.

As noted above, in theory, all 94 signatories to the Convention on Mutual Administrative Assistance in Tax Matters should eventually sign the MCAA (AEOI) to simplify implementation of AEOI.

And What Does All of This Mean?

Automatic exchanges of financial account information will commence during 2017 or 2018 depending on the commitment dates and achievement of the domestic requirements by the various countries. The financial information first exchanged in 2017 will cover the 12 month period ended 31 December 2016, whilst the 2018 exchange will first cover financial information for the 12 month period ended 31 December 2017.

As at 16 February, 2016 the list of countries and their declared first information exchange date are set out in the table at Annex 1.

In this regard we note that Singapore is not included in this list. That is, although it has committed to implement the CRS (to commence by September, 2018) it has not yet signed the MCAA (AEOI).

By comparison Indonesia has committed and has signed the MCAA (AEOI).

Related thereto we expect the 80 countries (and others that intend to follow) to legislate and/or regulate their domestic institutions to ensure that the necessary information is captured. In some cases this will increase the administrative burden at the time of opening bank accounts and other financial transaction accounts. In other cases existing account holders will be required to provide additional information to the relevant financial institution.

More importantly it will only be a matter of time before most financial centers have agreed to participate in AEOI. Any taxpayer that is resident of a participating country but relying on non-disclosure should expect to be questioned by their home tax authority if they do not resolve these non-disclosures.

Doing nothing will not solve the looming issues!

Automatic exchanges of financial account information will commence during 2017 or 2018 depending on the commitment dates and achievement of the domestic requirements by the various countries.

CbCR – Country-by-Reporting Reporting

CbCR refers to reporting under Action 13 of the BEPS Project. That is, it was identified that the tax authorities required a better understanding of the MNCs operating in their jurisdiction, against the background of the MNCs global operations. Thus CbCR is intended to assist the tax authorities when they consider the transfer-pricing activities of a qualifying MNC and whether there are potential mismatches/ BEPS strategies in play.

CbCR will be achieved by requiring MNCs to provide the following information, by country first (Table 1, irrespective of the number of companies within each jurisdiction) and then, within countries, indicate the main business activities of each company/ entity (Table 2).

In consideration of the administrative burden (and expectation of where BEPS activities might be most material) the threshold for CbCR are those MNC with consolidated revenues exceeding EUR 750 million, or a broad approximation of that amount in a country's local currency. Therefore CbCR will only be a concern for the largest MNC.

Table 1

Financial information/figures to be provided for each item

- Revenues (related party, unrelated party, total)
- P&L before tax
- Income tax – paid
- Income tax – accrued
- Stated Capital
- Accumulated earnings
- Number of employees
- Tangible assets other than cash

The threshold for CbCR are those MNC with consolidated revenues exceeding EUR 750 million .

Table 2

Check the box for each function performed

- R&D
- Holding/managing IP
- Purchasing/procuring
- Manufacturing/production
- Sales, marketing, distribution
- Admin, management, support
- Service provision to unrelated parties
- Internal group finance
- Insurance
- Holding company
- Dormant
- Other

MCAA – Multilateral Competent Authority Agreement re CbCR

The MCAA for CbCR was signed by 31 countries on 27 January, 2016 with Senegal signing later. (See Annex 2 for the list of the 32 signatories per 4 February, 2016.)

The MCAA (CbCR) allows for the automatic exchange of CbCR. As stated by the OECD Secretary-General Angel Gurría. "Under this multilateral agreement, information will be exchanged between tax administrations, giving them a single, global picture on the key indicators of multinational businesses. This is a much-needed tool towards the goal of ensuring that companies pay their fair share of tax, and would not have been possible without the BEPS Project."

First exchanges will start in 2017-2018 on 2016 information.

Once operational the tax authorities where an MNC operates will receive aggregate information relating to the global allocation of income and taxes paid, together with other indicators of the location of economic activity within the MNC. It will also cover information about which entities do business in a particular jurisdiction and the business activities each entity engages in. The tax authority of the country of residence of the MNC will be responsible for collecting the data and then exchanging this based on the MCAA or similar agreements.

Though, as noted above, this only applies to the largest MNCs.

What are the implications from the USA not signing the MCAA?

This is a good question, and in fact can be broadened and asked about the likely US response to the entire BEPS Project.

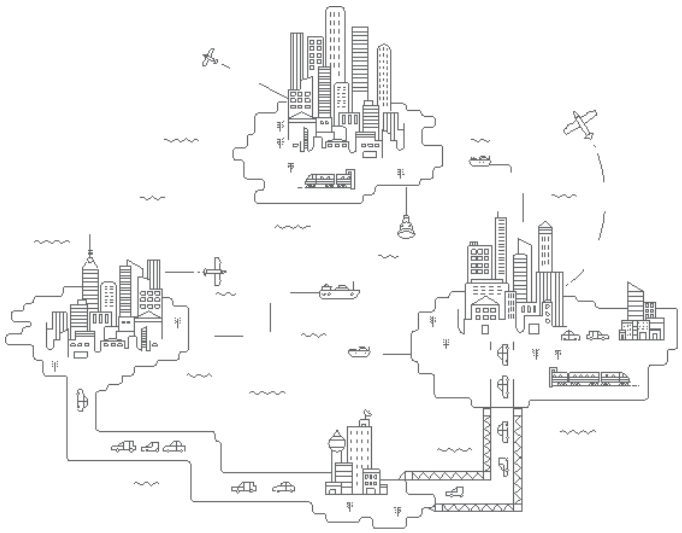
With respect to the AEOI, the US already has its FATCA and might, therefore, have limited interest in trying to synchronise this with AEOI. This would be unfortunate, although there is an analogy – accounting standards. The rest of the world (or at least most of it) has adopted IFRS, but the US maintains its own accounting system, US GAAP, and has pulled out of the convergence process that was established immediately post the GFC. Running FATCA and AEOI will duplicate costs for the economy and it would be hoped this could be avoided over the medium term.

But at present, FATCA is in place around the world and is operating, and AEOI is in the process of being rolled out. So, for at least the AEOI settling-in period, we should anticipate the two systems will run in parallel.

In the background, the OECD is quietly working on an 'exchange of everything' system – TRACE. Once that begins to roll out, it will supersede AEOI, and perhaps at that point FATCA will also be absorbed.

With respect to the US position on CbCR specifically, and the BEPS Project in general, this is a fascinating topic with no clear outcome. Throughout the BEPS Project, the US has been heavily involved at all levels within the OECD working groups. But in mainland US, there has been enormous antipathy towards the entire BEPS Project, with large business USA seeing the project as being directed against it. The Republican Party from time to time has come out against the Project.

And of course this is a Presidential election year, which under 'normal' circumstances would present challenges for significant foreign policy initiatives, but with the personality politics in play at present, it makes the outcome even more difficult to predict.



The IRS has issued proposed regulations to implement CbCR, and they are currently under review. There has been some argument as to whether the IRS has the power to implement CbCR by way of regulations, or whether the matter needs Congressional legislative action before implementation is possible. At present, the IRS view clearly is that it has the necessary power without the need to resort to Congress. Whether that view is challenged, or whether the proposed regulations are affected by the outcome of the Presidential election later this year, remains to be seen. But if the US companies were not to be subject to CbCR, then it would cause a degree of chaos in the global system, as most of the large affected MNCs are headquartered in the US, and the theory behind CbCR is that the parent company will prepare the CbCR and circulate it via the IRS to the Revenue Authorities of those jurisdictions within which it operates via branch or subsidiary.

Some countries which have already legislated for the introduction of CbCR, have built in alternative means of obtaining a copy of the CbCR. Australia for instance has placed the primary obligation to provide a CbCR on an Australian subsidiary of an affected MNC. However, that primary lodgment obligation is lifted if the parent provides a CbCR by way of IRS exchange. Other countries are likely to follow a similar path, although the quality and breadth of a CbCR provided by an MNC subsidiary may be questioned.

Finally, in relation to the US response to the BEPS Project generally, its position on the Multilateral Instrument will be very interesting given its key role in the global economy.

Throughout the BEPS Project, the US has been heavily involved at all levels within the OECD working groups.

The IRS has issued proposed regulations to implement CbCR, and they are currently under review.

Double Tax Agreements/Tax Treaties (DTA)

The BEPS project has recommended the revision to the OECD Model Tax Convention for DTA. In conjunction with Multilateral Instrument under BEPS Action 15 it is likely that countries will seek to update their existing in force DTAs. It is expected that this will remain a negotiation process between the treaty partners.

In theory the closer the parties are to the OECD MTC then the simpler the negotiation. In practice even OECD countries are likely to continue to reserve certain rights/issues based on their domestic laws and positions. The negotiations may be more tortuous where the existing DTA is closer to the UN Standard rather than the OECD MTC.

Irrespective the process of working through each country's DTA with the respective partner (who is doing the same with their other treaty partners) will be a time consuming exercise that is likely to prioritise the major trading partners.

The BEPS project has recommended the revision to the OECD Model Tax Convention for DTA.

Annex 1. Countries that have signed the MCAA (AEOI) – 16 Feb 2016

Jurisdiction	Intended month of first information exchange
Albania	September 2018
Andorra	September 2018
Anguilla	September 2017
Antigua and Barbuda	September 2018
Argentina	September 2017
Aruba	September 2018
Australia	September 2018
Austria	September 2018
Barbados	September 2017
Belgium	September 2017
Belize	September 2018
Bermuda	September 2017
British Virgin Islands	September 2017
Bulgaria	September 2017
Canada	September 2018
Cayman Islands	September 2017
Chile	September 2018
China	September 2018
Colombia	September 2017
Cook Islands	September 2018
Costa Rica	September 2018
Croatia	September 2017
Curacao	September 2017
Cyprus	September 2017
Czech Republic	September 2017
Denmark	September 2017
Estonia	September 2017
Faroe Islands	September 2017
Finland	September 2017
France	September 2017
Germany	September 2017
Ghana	September 2018
Gibraltar	September 2017
Greece	September 2017
Greenland	September 2017
Grenada	September 2018
Guernsey	September 2017
Hungary	September 2017
Iceland	September 2017
India	September 2017
Indonesia	September 2018
Ireland	September 2017
Isle of Man	September 2017
Italy	September 2017
Japan	September 2018
Jersey	September 2017
Korea (South)	September 2017
Latvia	September 2017
Liechtenstein	September 2017
Lithuania	September 2017
Luxembourg	September 2017
Malaysia	September 2018
Malta	September 2017
Marshall Islands	September 2018
Mauritius	September 2017
Mexico	September 2017
Monaco	September 2018
Montserrat	September 2017
Netherlands	September 2017
New Zealand	September 2018
Niue	September 2017
Norway	September 2017
Poland	September 2017
Portugal	September 2017
Romania	September 2017
Saint Kitts and Nevis	September 2018
Saint Lucia	September 2018
Saint Vincent & the Grenadines	September 2018
Samoa	September 2018
San Marino	September 2017
Seychelles	September 2017
Sint Maarten	September 2018
Slovak Republic	September 2017
Slovenia	September 2017
South Africa	September 2017
Spain	September 2017
Sweden	September 2017
Switzerland	September 2018
Turks & Caicos Islands	September 2017
United Kingdom	September 2017

Annex 2. Countries that have signed the MCAA (CbCR) – 4 Feb 2016

Jurisdiction
Australia
Austria
Belgium
Chile
Costa Rica
Czech Republic
Denmark
Estonia
Finland
France
Germany
Greece
Ireland
Italy
Japan
Liechtenstein
Luxembourg
Malaysia
Mexico
Netherlands
Nigeria
Norway
Poland
Portugal
Senegal
Slovak Republic
Slovenia
South Africa
Spain
Sweden
Switzerland
United Kingdom

RSM in Indonesia

6th
largest global audit, tax
and consulting network

760 offices

120 countries

38,000 people

RSM is the world's 6th largest network of audit, tax and consulting firms. We have more than 760 offices in more than 110 countries. Worldwide, we are supported by more than 38,000 staff.

RSM is represented in Indonesia by the following member firms: Amir Abadi Jusuf, Aryanto, Mawar & Rekan; PT RSM Indonesia Konsultan; PT RSM Indonesia Mitradaya; PT RSM Indonesia Mitradana. RSM's Indonesian member firms work closely together within Indonesia. Each firm is a separate and independent legal entity and a member of the RSM network and trades as RSM. RSM is the trading name used by the members of the RSM network.

We have been operating for 30 years in Indonesia, and RSM has been operating globally for 50 years.

RSM in Indonesia was established in 1985 and become part of RSM in 1992. Since its establishment, it grew to be an integrated professional services firm of AAJ Associates, then RSM AAJ, and now RSM Indonesia.

·Passing 3 decades of presence in Indonesia, we are able to grow our staff from just 3 people back in 1985 to 600 during the busy seasons; established offices in Jakarta and Surabaya, and we are positioned at the 5th place in Indonesia among audit, tax & consulting firm alike.

We assists many organizations in Indonesia through providing audit, tax, and advisory services, including cross-border listings.

For the last 10 years we stably ranked 3rd in the number of listed companies in Indonesia that were audited by us.

The Author

Nicholas Graham is a Tax Partner at RSM in Indonesia. He has over 25 years of experience in his field assisting various types of companies.

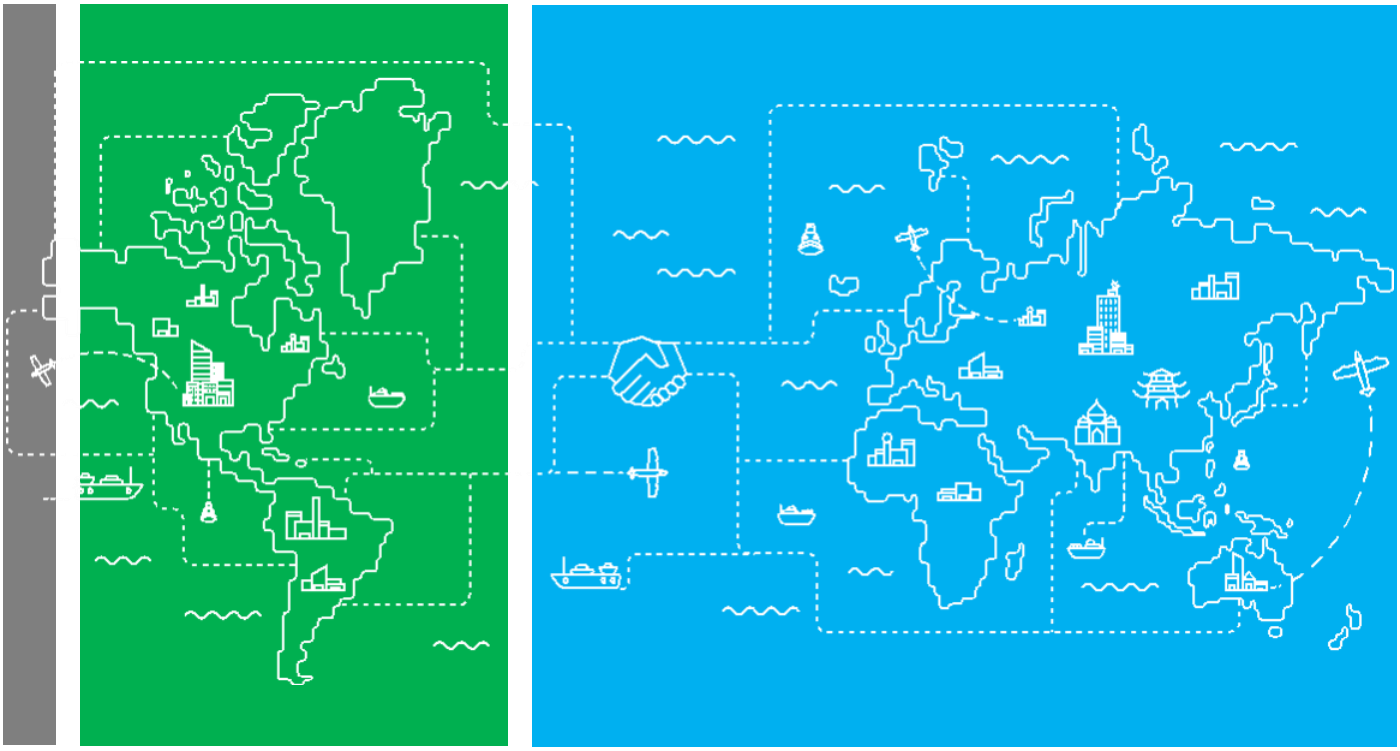
Nick is a qualified Chartered Accountant having completed the Professional Year program of the Institute of Chartered Accountants of Australia, and he is a Fellow of the Financial Services Institute of Australasia (FinSIA).

He is active in the management of Australia-Indonesia Business Council network. He earned his Bachelor degree of Business from the University of Technology, Sydney, Australia and also holds a Graduate Diploma of Applied Finance from the Financial Services Institute of Australasia.

For further information, please contact

nick.graham@rsm.id

This paper is prepared by Nick Graham with review and input by Craig Cooper of RSM Australia. Information for this article is obtained from various sources. In addition to the RSM network key definitions and explanations of the developments are sourced from the OECD's Centre for Tax Policy and Administration webpages and articles.



Thank you for reading.

RSM

Plaza ASIA Level 10
Jl. Jend. Sudirman Kav. 59
Jakarta 12190 Indonesia

www.rsm.id

RSM