

# The Case Against BEPS: Lessons for Coordination

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# Outline

- Why BEPS now?
- Problematic Premises
- Lead to Poor Outcomes
- Addendum: Recent Developments

# What is BEPS

- Action plan to combat base erosion and profit shifting by multinational enterprises
- 15 “action items”
- Supposed to prevent multinationals’ profits from being able to obtain status of “double non-taxation” or “stateless income”

# BEPS Recommendations

- Recommendations for changes in domestic laws
  - Interest expense deductibility
  - Hybrid Instruments
- Revisions to treaties (MLI, principal purpose test)
- Modifications to the OECD transfer pricing guidelines
- Transparency, exchange of information, harmful tax practices
- Studies and reports not recommending particular rule changes
  - Digital economy
  - Quantifying BEPS

# Why BEPS Now?

- Inequity and the financial crisis
- Digital Economy
- Political Cover for Politicians
- Global Power Shifts
- The OECD's role

# Weak Foundations

- Coordinated effort mostly ignored the underlying issues that gave rise to the challenges that the project was supposed to address
- Global Politics
  - No agreement on allocation
  - Challenges of focusing on value creation
  - Source v residence
  - Shifts in balance of power

# Weak Foundations

- Domestic Politics
  - Power to tax = political power
  - Need to encourage investment
    - Patent box
- Value Creation
  - Never defined
  - Never acknowledged its departure from prior principles

# Poor Outcomes

- Minimum standards or lack thereof
  - Four minimum standards
- U.S. Non-Participation
- Digital Economy
- Other hard questions pushed aside (profit split, attribution of profits)
- Vague Rules
  - Transfer Pricing Guidelines: Deliberate Incoherence?
  - Permanent Establishment Standard

# Conclusion

- Differing objectives among participants led to unsatisfactory outcomes
- Attempts at coordination led by developed countries are doomed to be unsuccessful because they lack full participation from non-OECD global economic players, are based on incoherent principles, and fail to take account of strong nationalist interests
- To really address the larger (unacknowledged) challenges, need a reexamination of underlying principles and broad agreement on such principles
- Need to formulate goals for an international tax system that take into account both global inequalities and the benefits countries obtain from tax competition

# Addendum – Subsequent Developments

- Digital Economy:
  - Top priority item now revived with draft recommendations due next April
  - No closer than they were 2 years ago
  - Focus on short term to “keep the pressure cooker from exploding”
  - But the U.S. seems unlikely to agree to any proposed solution
  - Interaction with U.S. tax reform – could make BEPS moot?

# Addendum – BEPS Implementation

- Multilateral instrument: principal purpose test
- Country by country reporting
- Gary Sprague presentation at digital economy consultation: BEPS is having an impact and new PE definition is prompting companies restructure their distributorship operations

# Addendum: US Tax Bill

- Anti-base erosion measures
- Competitive lower corporate rate
- Spillover effects