OECD Action Plan on International Tax Avoidance

Action Plan on Base Erosion and Profit Shifting

This is a quick summary of the 2013 Action Plan available here.

The OECD recognized the need to act in order to maintain the functioning of the current consensus approach of international taxation, and to prevent unilateral action by countries so as to protect their tax bases. The increasing pace of global economic integration, large use of multi national enterprises, and the growing digital economy have highlighted the mismatches, frictions, gaps and loopholes of the current system. Such deficiencies have allowed for tax avoidance and arbitrage opportunities that harm countries, individuals, and small/local businesses.

In order to deal with the international tax system's deficits, international cooperation and coordination in developing coherent domestic and international tax rules/principles is required. The major aim of this cooperation and coordination is dealing with (1) double non-taxation, (2) less than full taxation of cross-border income, and (3) the separation of value creation and income recognition and economic activity.

The OECD has set up a task force to identify the manner in which the digital economy creates value and makes profits. this greater understanding will fill a knowledge gap that will be used to assess changes needed in domestic and treaty rules so as to properly align taxation and economic activity that creates value. This, however, will not result in a change in existing international norm of allocating taxing rights of cross border income.

The outcomes expected include:

- introduction of standards to deal with the artificial segregation of taxable income and underlying economic activity
- developing rules to deal with third parties inserted in bilateral tax treaty arrangements, where third parties add little to no value but obtain disproportionate allocation of income
- adapt transfer pricing rules to emphasise value creation in integrated groups and limit the use of intangibles, risk, capital, and other arrangements to shift profits
- introduce systems to obtain timely, comprehensive, and relevant information on tax planning strategies, including mandatory disclosure by business of tax planning methods, income allocation, taxes paid, and economic activity within integrated groups
- introduce greater corporate tax coherence internationally through changes in domestic and treaty rules
- prevent hybrid mismatch arrangements that allow for double deductions on one borrowing, deductions without corresponding inclusions, misuse of foreign tax credits, and abuse of exemption regimes
- development of comprehensive controlled foreign corporation rules
- develop rules to address abuses using debt, risk, and derivatives
- develop an approach to deal with harmful regimes that fuel a race to the bottom in taxing

certain types of income
- introduce anti-treaty abuse rules to prevent treaty shopping and treaty arbitrage
- change rules relating to permanent establishment rules and exceptions thereto to deal with abuses in corporate groups, and
- develop transfer pricing rules to deal with arms length principles in relation to intangibles and arrangements that would rarely occur between third parties.

These action plans raise interesting questions as to approaches possible, particularly in the area of rethinking the basis of taxable income allocation on the basis of value creation indicators.

The OECD has provided a timeline wherein the majority of the actions will be taken and implemented within 2 years.

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