Global Financial Services view on BEPS – webcast series

Latest developments of relevance to asset managers

Monday 17 October, 9–10am EDT/3pm CEST

Notice

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Agenda and speakers

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Transfer Pricing: Actions 7, 8–10 and 13

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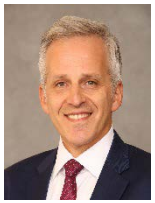
Transfer Pricing: Actions 7, 8–10 and 13



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OECD policy developments

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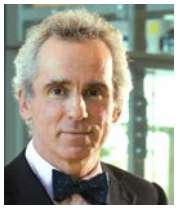
EU developments



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Notes on CPE and polling questions

Continuing Professional Education (CPE) Credits

North America

— We require that participants are registered, logged in and take part in at least 4 of the 5 polling questions and participate in at least 50 of the 60 minutes to qualify for CPE credits for today's webcast.

Outside North America

— We encourage you to participate in the questions, as you may be eligible for continuing education credits in your local jurisdiction.

Polling Questions

— Polling questions will appear as we proceed through the presentation.

— As mentioned, in order to receive the CPE credit, we require that those participants take part in at least 3 of the 5 polling questions and participate in at least 50 of the 60 minutes to qualify for CPE credits for today's webcast.

Questions

— You may submit questions in the 'Ask a question' button on the left. We will answer as many questions as we can during Q&A. If we are unable to answer your question, someone from KPMG may reply via phone or email.

— For technical issues, please use the Question Mark button in the upper-right hand corner of the media player.

Your feedback

— When the webcast is over, the webcast player will automatically refresh to display an exit survey. Feel free to complete the survey, as your comments are very valuable to us.

Polling question #1

How do the Board and C-level management of your company perceive the significance and potential impact of the BEPS Action Plan?

A

Concerned — They have a high-level understanding and are engaged and interested

B

Aware — They understand it, and there is some dialogue about it, but they are not concerned

C

Passive — They are aware of the debate but are neither concerned nor engaged in regular dialogue about it

D

Not aware — They are not aware of the BEPS Action Plan

E

I do not know

Transfer pricing: Actions 7, 8 and 10

John Neighbour

Sherif Assef

BEPS Action 7

Art. 5(5) Conclude contracts

Activities that may habitually conclude contracts or habitually playing the principal role leading to conclusion of contracts routinely concluded without material modification?

- Relationship banking
- Sales and origination
- Trading
- Product distribution
- Investment management
- Asset acquisition/disposal negotiation
- Travelling underwriters
- Other short term business travellers

Art. 5(6) Independence requirement

A person acting exclusively or almost exclusively on behalf of one or more enterprises to which it is connected ('50% test') shall not be considered independent

Recent developments

Attribution of Profit to PEs Discussion Draft

— Discussion draft released on 4 July 2016 on how the attribution of profits to permanent establishments ('PEs') under Article 7 of the Model Tax Convention ('MTC') should take account of the changes in the final BEPS reports to both the PE definition and the Transfer Pricing Guidelines.

— The discussion draft is focused on two areas:

a) dependent agent PEs ('DAPEs'); and

b) warehouses as fixed place of business PEs.

— It takes the form of 4 examples relating to DAPEs and one example relating to warehouses.

— Each example is followed by specific questions to commentators.

— The discussion draft also discusses the coordination of Articles 7 and 9 of the MTC.

— Comments were submitted through early September 2016, and the OECD held a public consultation in Paris on 11–12 October 2016.

Action 8-10 – Transfer pricing (Aligning outcomes with value creation)

Legal ownership of an intangible does not provide a right to all (or any) of the return on the intangible

— Returns accrue to entities that carry out **D**evelopment, **E**nhancement, **M**anagement, **P**rotection, and **E**xploitation (DEMPE) functions attributable to that intangible

Risk and Capital

— An entity providing only capital will be entitled to no more than a risk-free return

— Taxpayers may need to provide evidence that they have appropriate people, in the right locations, with the skills to deploy capital and assume risk

Take Aways…

— Analyze each risk and confirm that the allocation of risk is reflected in written contracts and the conduct remains aligned with contractual terms

— Expect time-consuming and costly disputes to increase — consider APAs or other dispute resolution mechanics

Recent developments: Profit split method

Discussion draft released on 4 July 2016 addresses follow-up work and proposes revised guidance on the application of the transactional profit split method as well as addresses several of the comments gathered on the prior discussion draft.

— New discussion on two broad ways of splitting profits — splitting actual profits or splitting anticipated profits.

— Emphasizes the role of risk-sharing or the integration of risks between related parties as an important factor in the determination of whether a profit split is appropriate, thus tying the discussion back to the guidance on risk in Chapter I.

— The discussion draft discusses both strengths and weaknesses of the profit split method, and also adds some discussion of situations where a profit split approach might not be most appropriate. The OECD, thus, tried to address concerns expressed by commentators on the first discussion draft on potential overuse of profit splits.

— The discussion draft makes it clear that a lack of comparables alone is insufficient to warrant the use of a profit split.

Despite some cautionary language in the draft on when tax authorities might seek to apply a profit split, taxpayers will continue to be wary.

Polling question # 2

Is the OECD guidance on use of the profit split or treatment of risk & capital causing you to rethink aspects of your transfer pricing policies?

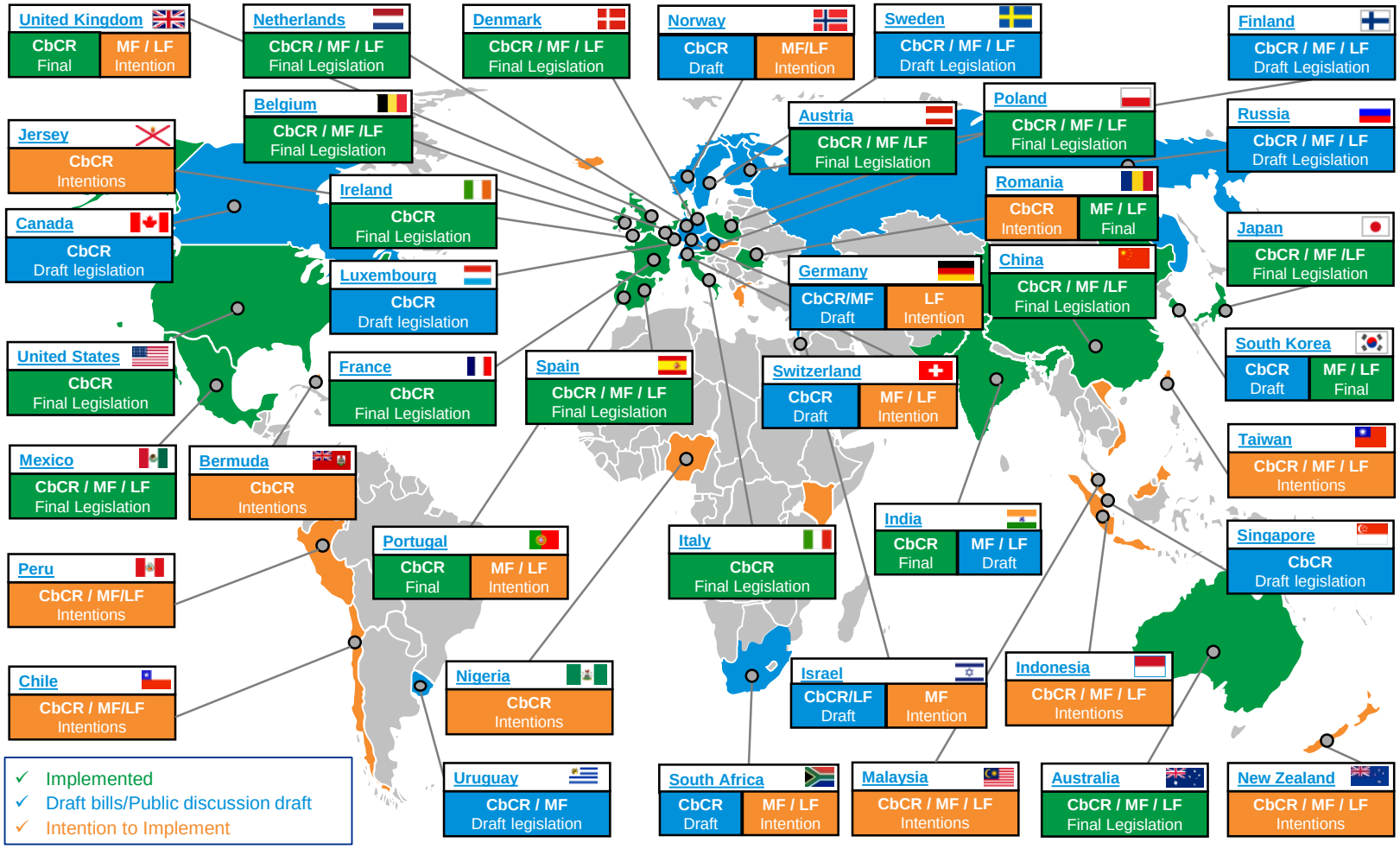
A	B	C
Yes	No	Not sure

Action 13 – Country by Country Reporting

Sherif Assef

Michael Plowgian

BEPS Action 13: Country implementation summary



Source: KPMG International 2016

Interaction between the three elements of Action 13

Country-by-country reporting

1. Country-by-country breakdown of global income, taxes paid, and certain indicators of economic activity (*e.g.*, assets and headcount).
2. List of all entities, branches and permanent establishments and indication of their economic activity.

MF puts CbCR in global context

LF puts CbCR in local context

Master file

1. Overview of the multinational entity (MNE) group business.
2. Global value chain analysis.
3. All information should be available to all applicable tax authorities.

Local file

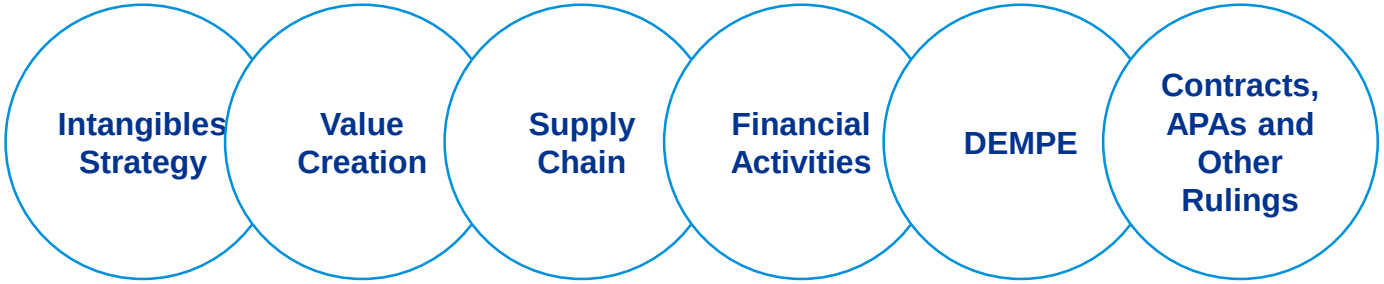
1. Information relevant to the transfer pricing analysis of a local entity.
2. Details of specific intra-group transactions.

CbyC reporting: New OECD guidance

- No exemption for investment funds
- Definition of MNE Group based on accounting consolidation rules
- Treatment of partnerships
- Voluntary “parent surrogate” filings
- Impact of currency fluctuations

Master file: What is different?

1. This is not your status quo documentation of the past, it is NEW and DIFFERENT — it is a more complete organizational picture compared to what has been presented in the past to tax authorities.
2. May be required by tax authorities in all countries in which the MNE operates.
3. Will require concerted effort to craft a complete, consistent and coherent story.



4. The Master File requirements warrant considerable thought to develop:
   a. Master File is an opportunity for taxpayers to tell their story first and offers a first-mover advantage when dealing with tax authorities.
   b. On the other hand, the more information provided in the Master File the more potential issues with consistency with other information and information security.
5. There are other stakeholders outside the tax function that will likely need to be included in the development and review of a Company's Master File.

Timeline – so when should I start?

- Year ended December 2016 is generally first year relevant for:
  - Country by Country Reporting
  - Master File
  - Local File
- Natural order of preparation is:
  - 1st CbCR — to understand the raw financial data and likely analytics tax authorities will perform
  - 2nd Master File — to articulate the key messages that will explain the allocation of profit
  - 3rd Local File — to explain the local contribution to the value chain consistent with the key messages in the Master File

  But,
  - For many tax payers, the deadline for submitting the relevant Local File (and Master File) will be the most pressing!

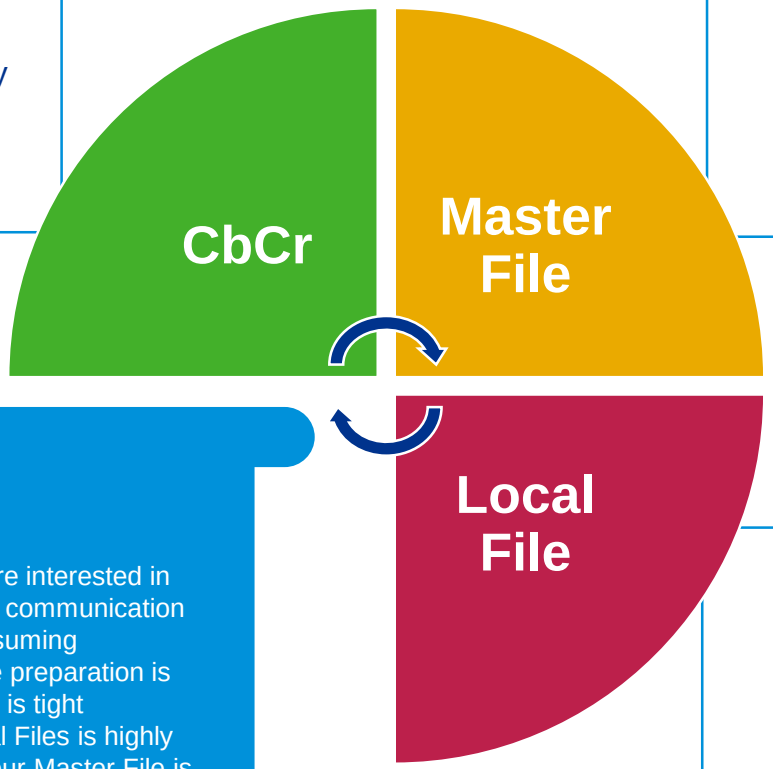
Timeline – so when should I start?

An example — Chinese subsidiary, with Local File deadline of June 2017

Dec 2016

— Prepare CbyC data
— Implement necessary changes to TP policies pre-year end

— Document Value Chain Analysis
— Determine key messages
— Prepare Master File



Sept 2016

Mar 2017

Key learnings so far:

— Many stakeholders are interested in changes in pricing — communication internally is time consuming
— CbCr and Master File preparation is complex — 3 months is tight
— The structure of Local Files is highly dependent on how your Master File is structured

June 2017

— Document local operations in accordance with Local File requirements

Source: KPMG International 2016

Polling question #3

Are you confident that you will be able to meet Action 13 requirements to the extent that they are contemporaneous?

A	B	C
Yes	No	Somewhat

OECD policy developments

Michael Plowgian

BEPS Action 2

OECD Discussion Draft on Branch Mismatch Structures

- On August 22, the OECD released a Discussion Draft on branch mismatch structures.
- Branch mismatches occur where the residence and branch jurisdictions take a different view as to the allocation of income and expenditure between the branch and the head office, and include situations where the branch jurisdiction does not treat the taxpayer as having a taxable presence in that jurisdiction.
- Also addresses imported mismatches.
- Issues raised in Action 6 triangular provision, US Model Tax Treaty, state aid investigations.
- Viewed as addressing arrangements that are similar in effect to those targeted by the final Action 2 report.

BEPS Action 4

OECD Discussion Draft on Approaches to Address BEPS Involving Interest in the Banking and Insurance Sectors

- On July 28, the OECD released a Discussion Draft on approaches to address BEPS involving interest in the insurance and banking sectors. The Discussion Draft does not recommend specific action by OECD member countries.
- The final report will describe existing approaches taken by countries to limit the deductibility of interest by banks and insurance companies.
- The final report may also provide additional guidance regarding the application of the fixed ratio rule and group ratio rule to non-regulated entities in insurance or banking group.
- Apply the fixed ratio rule separately to regulated and non-regulated groups of entities.
- Apply higher fixed ratio within 10%–30% range.
- Apply fixed or group ratio rule by excluding the EBITDA or net interest position of regulated entities.
- Where interest expense is incurred in non-regulated entities to support regulated activities, exclude some or all of the third party interest expense from the net interest expense subject to the rule.
- Comments concerned about impact on non-regulated entities in groups with regulated entities.
- Ability to use non-regulated entities to finance the group or related entities?
- How to allocate interest expense among regulated and unregulated activities of the group?

BEPS Action 15

Multilateral instrument

Work on multilateral instrument

- Text of multilateral instrument has been agreed; text likely to be released after formally adopted in November.
  - Overall structure of the instrument includes:
    - Provisions implementing each of BEPS tax treaty-related measures — Action 2 (Hybrid Mismatches), Action 6 (Preventing Treaty Abuse), Action 7 (Preventing Artificial Avoidance of a PE), and Action 14 (Improving Dispute Resolution);
    - An optional provision on mandatory binding arbitration;
    - A flexible approach, with opt-ins, alternatives, and opt-outs (except for minimum standards (mainly Actions 6 and 14) to allow countries to follow their unique tax policy preferences; and
    - A series of notifications to ensure clarity on how the MLI will modify the operation of provisions in existing tax treaties;
    - Treaties amended on bilateral basis.
- Further Work on Action 6 (Treaty Abuse) and Non-CIVs.

Polling question #4

Do you think the BEPS initiative will ultimately increase your organization's Effective Tax Rate?

A	B	C
Yes	No	Not sure

Actions 6 & 12

Andreas Patzner

BEPS Action 6 – Treaty abuse

Summary

- The final report includes draft provisions for both a US-style LOB and for a “simplified” LOB. The simplified LOB is expected to be paired with the PPT. Further work has been done on both the detailed and simplified LOB and Commentary during the first part of 2016, in light of changes to the U.S. model LOB.
- Treatment of Collective Investment Vehicles to be bilaterally agreed, may be viewed as automatically “qualifying persons” for purposes of the LOB Test.
- Contracting states who go with the LOB option are to bilaterally agree how “CIV” should be defined.
- Also to agree whether they will make it easy or difficult for CIVs to fall within the definition of “qualified persons” in their specific tax treaty. Will all CIVs be “qualifying persons” or only those that meet certain ownership tests?
- If CIV qualification is to be conditional then implementation of the TRACE project is important.
- No immediate conclusions on non-CIVs. Further work to be done.
- Pension funds to be provided with “resident” status

Issues for consideration

- Lack of uniformity with regard to the treatment of CIVs, the definition of CIVs and their entitlement to treaty benefits. Will create complexity and uncertainty.
- Bilateral negotiation required to finalize CIV treatment on a treaty by treaty basis where LOB approach adopted.
- EU countries most likely to adopt PPT in preference to LOB test.
- Will States take different approaches to the timing of implementing the TRACE project?
- Uncertainty for non-CIVs due to deferred decision on treatment.

BEPS Action 12 – Disclosure of tax planning

Summary

- The final report of 5 October 2015 provides a modular framework that enables countries without mandatory disclosure rules to design a regime that fits their need to obtain early information on potentially aggressive or abusive tax planning schemes and their users.
- No minimum standard, countries are free to choose whether or not to introduces mandatory disclosure regimes.
- Specific recommendations for rules targeting international tax schemes, information exchange and co-operation between countries.
- It seems that countries do already implement first disclosure mechanism.
- e.g. Germany has launched a legislative draft to oblige tax advisors of foreign and German funds to disclose potentially aggressive tax schemes which influence the taxation of German fund unit holders (German Investment Tax Reform Act which has passed parliament on 9 June 2016).

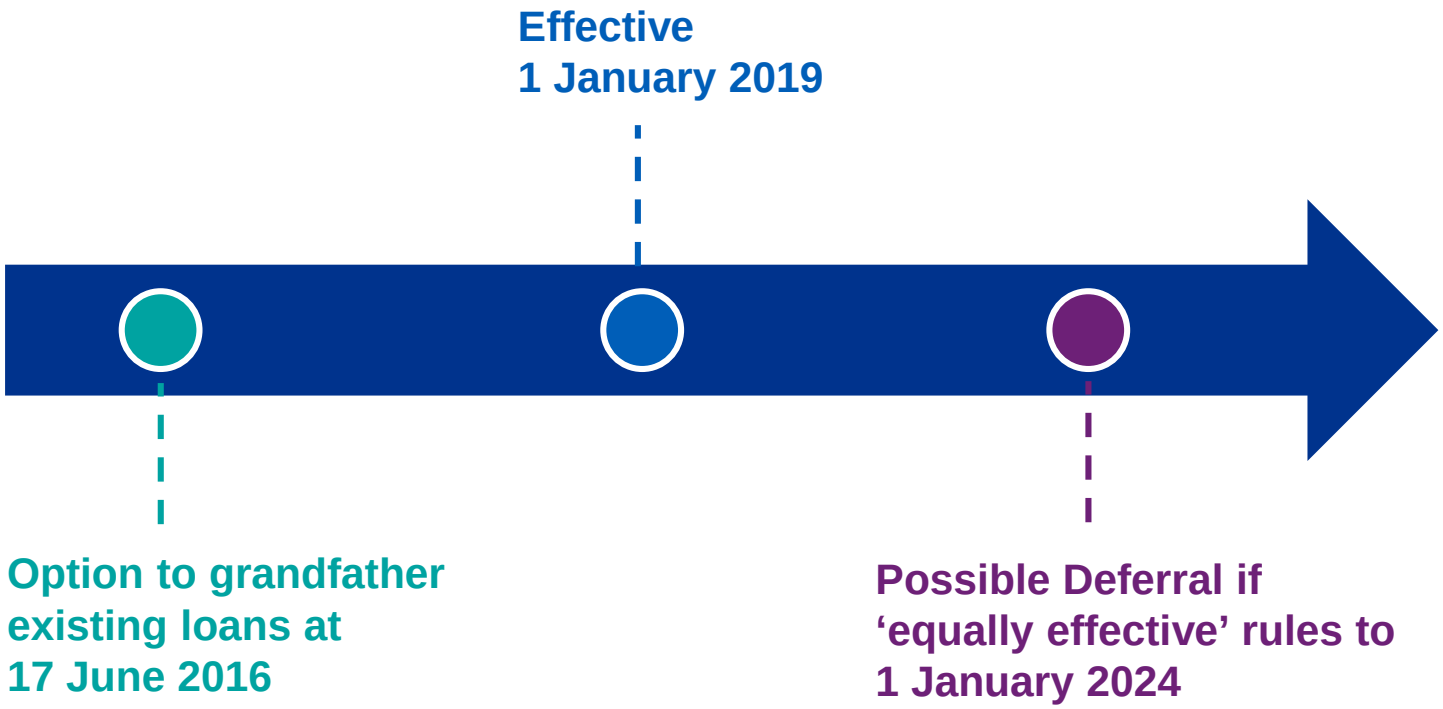
Issues for consideration

- Who has to report? Investment Manager, Funds, (Tax) Advisors.
- What has to be reported? Reportable Schemes and Arrangements. (Countries to decide)
- When is information to be reported?
- What are the consequences of non-compliance?
- What are the consequences of disclosure?
- Funds involved in the dividend-trades (cum-cum or cum-ex)

EU developments

Barry Larking

Interest restriction



Source: KPMG International 2016

Interest restriction

Optional exemption for financial undertakings

- Credit institutions (banks)
- Insurance/Reinsurance companies
- Occupational retirement pension funds
- EU social security pension schemes
- AIFMs. AIFs managed by AIFMs, supervised AIFs
- UCITS funds
- OTC derivative counterparties

Source: KPMG International 2016

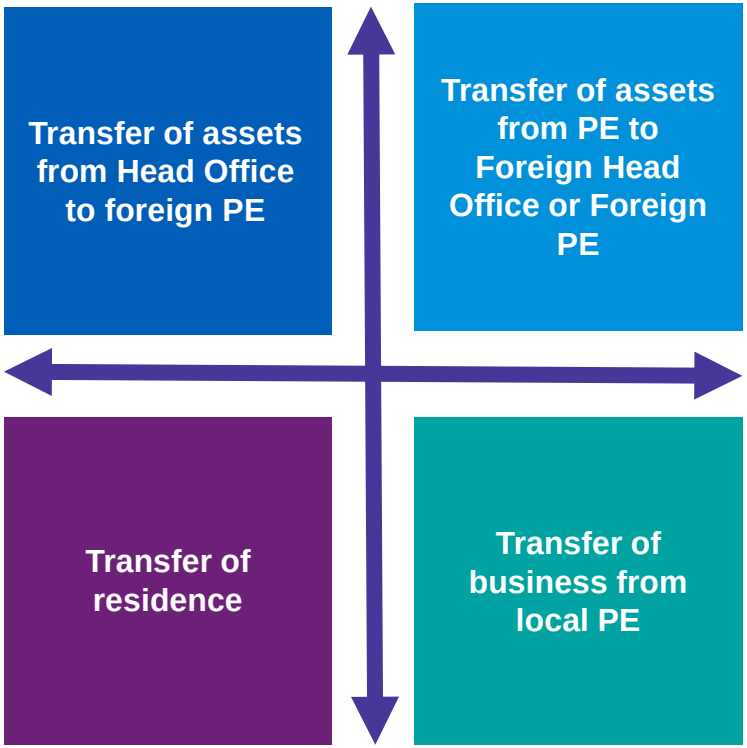
Exit charge

Deemed disposal at market value where Member State loses taxing rights as a result of:

Deferral + interest/guarantee for EU/EEA transfer

Exclusion for <12 month transfer for:

- Financing of securities
- Collateral
- Prudential capital requirements
- Liquidity management



Option to Defer Implementation until 2020

Source: KPMG International 2016

Controlled foreign company (CFC) rule

CFC =
Sub or PE
EU or non-EU

Listed passive income

Diverted SPC income

Source: KPMG International 2016

Controlled foreign company (CFC) rule

Category approach — Non distributed

- Interest & income from financial assets
- Royalties & IP income
- Dividends
- Gains on shares
- Finance lease income
- Insurance, banking and financial activity profits
- Limited-risk distribution/ commissionaire profits

Substantive economic activity exclusion EU (+maybe non-EU)

Financial Undertakings ≤1/3 income in specified categories from Head Office or 25%+ associates

Source: KPMG International 2016

General anti-abuse rule (GAAR)

Ignore arrangement

Main purpose: Tax advantage	**Defeats object /Purpose of law**	**No valid commercial reasons/ economic reality**

Source: KPMG International 2016

Anti-hybrid rule

EU member states only

PSD anti-hybrids not affected

No reverse hybrids

No branches/PEs

No dual residents

Source: KPMG International 2016

More to come?

EU	Beneficial ownership registers, mandatory disclosure rules, protection of whistle blowers.
OECD	Multilateral Instrument expected 1st half 2017 to implement BEPS treaty actions (e.g. PE's, Anti-avoidance, Dispute resolution, Hybrids)
EU	"Black-list" of non-EU 'non-cooperative' jurisdictions (end 2017)
EU	Automatic exchange of tax rulings (DAC 3): from 1 January 2017
EU	Country-by-Country Reporting (DAC 4) (OECD Action 13 CBCR) from July 2018 (for 2016)
EU	Public CBCR Proposal for ALL sectors
EU	Tax authority access to AML information including UBO details (DAC 5)
EU	ATAD 2: anti-hybrid rules for PE's and third countries
EU	Dispute resolution proposal (November 2016)
EU	Guidelines on conditions and rules for issuance of rulings (Code of Conduct)
EU	New Common (Consolidated) Corporate Tax Base proposal (November 2016)
EU	State aid……

Polling question #5

Would you like to be contacted by a KPMG professional to discuss the impacts of BEPS on your organization?

A	B
Yes	**No**

KPMG

Q&A

Thank you! Please contact us with any questions.

Moderator

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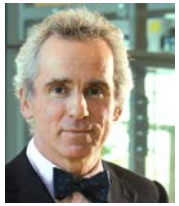

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