



# Is tax planning possible in the era of BEPS and MLI?

ICAI - National Conference on International Tax

Hitesh D. Gajaria

January 2020

[home.kpmg.com/in](http://home.kpmg.com/in)

# Is tax planning still possible?

1	The Context	
2	Traditional areas of tax planning	
3	Overview of relevant BEPS / MLI measures	
4	The Impact of BEPS / MLI measures	
5	Takeaways	

# The Context

# The Context

1

## Origins of State Sovereignty

- Treaty of Westphalia (1638)
- Gradual expansion of tax regimes, specially taxation of income / profits
- Taxing rights based on a Country's relationship to the subject of the tax (i.e. the citizen or resident) OR the object of the tax (i.e. the source of income)
- Countries typically levy tax on all incomes of residents and locally-sourced income of non-residents
- Rare Overlapping of tax claims

2

## Interaction of national tax systems (1920 - date)

- Outcome of increased cross-border trade; people mobility
- Rise in Overlapping tax claims resulted in double taxation leading to pressures from businesses
- Arrangements involving bilateral co-ordination put in place under the aegis of the League of Nations:
  - Countries accepting limitations on their sovereign taxing rights; AND
  - Enabling co-ordination via network of bilateral tax treaties (over 3,000)

3

## ...the emerging era

- Rise of Multilateral efforts to tackle key challenges
  - Increased Unilateral and Protectionist actions in areas such as tax cuts, base erosion payments, digital economy taxation etc.
  - Emergence of new factors that affect tax decision-making
  - Decades-long stability of the global tax system under upheaval
- Future of 'tax planning' under question**

# Traditional areas of tax planning

# Traditional areas of Tax Planning

## Supply Chain

- IP and R&D planning (contract R&D, cost sharing arrangements etc.)
- Tax-efficient manufacturing arrangements (e.g. contract and toll manufacturing)
- Sales and distribution arrangements (dependent and independent agents, marketing support, limited risk and full distributors, commissionaire structures)

## Holding / Financing Structures

- Accessing treaty benefits through use of holding companies in favourable jurisdictions
- Funding structures, including through use of inter-company debt
- Use of group financing entities and branches
- Hybrid instruments

## Incentive Regimes

- Headquarter regimes
- IP and other R&D incentive regimes (including patent box, IP box regimes)
- Deemed foreign tax credit regimes
- Participation exemption

# Overview of relevant BEPS / MLI measures

# Key focus areas of the BEPS / MLI initiatives



# Impact of BEPS / MLI on tax planning

# Impact of BEPS / MLI on Tax Planning

## Supply Chain (R&D / Manufacturing)

- Increased focus on aligning taxation with value creation (especially w.r.t. intangibles):
  - Intended to prevent companies not having significant employees or minimal operations from earning significant risk-related or intangible-related returns
  - Contractual arrangements or funding to not by themselves entitle an entity to returns from intangibles or risk assumption
  - The entity must have “substance” in the form of actual controlling of risk by employees or by performing of important DEMPE functions

### Impact on planning

- Pure ‘cash box’ entities may no longer work
- Need to shift IP / intangibles to entities with employees and operations (i.e. substance)
- Need to shift employees and operations to entities with IP / intangibles
- Increased availability of information with the tax authorities under CbCR

# Impact of BEPS / MLI on Tax Planning

## Supply Chain (Marketing/Distribution)

- Scope of PE expanded to include agent playing principal role, leading to routine conclusion of contracts, without material modification
  - Agent acting exclusively or almost exclusively on behalf of one or more closely related enterprises not to be considered independent
  - Restricted exemptions for preparatory and auxiliary activities under some treaties
  - Restriction on splitting up of contracts for installation PE
- Impact on planning**
- Increased focus on actual conduct in the source state
  - Planning involving use of structures where final signing / approval authority is retained outside the source country could be affected
  - Artificial splitting up of contracts to be disregarded for computing installation PE thresholds

# Impact of BEPS / MLI on Tax Planning

## Holding and Financing Structures

- Several measures intended to curb ‘treaty shopping’
  - Changes to the treaty preamble
  - Introduction of a Simplified Limitation on Benefits Article (and a detailed LOB with anti-conduit rules)
  - Use of a ‘Principal Purpose Test’ to access treaty benefits
- Proposals to neutralize hybrid mismatch arrangements
- Thin-capitalization provisions

### Impact on planning

- Treaty access for holding / financing SPVs at risk – several existing structures could be affected
- ‘Purpose’ behind structures will be critical going forward
- Domestic law provisions may be introduced denying deductions if income itself is exempt
- Thin capitalisation provisions will affect debt financing structures in high tax jurisdictions

# Impact of BEPS / MLI on Tax Planning

---

## Incentive Regimes

- Harmful tax practices – incentive regimes under scrutiny at the OECD
- State-aid cases under EU Anti-Trust rules
- Pillar Two Proposals – move towards a Global Minimum Tax

## Impact on planning

- Continued availability of incentives (headquarter regimes, private rulings, deemed credit etc.) under a scanner
- Tax benefits could face challenges under anti-trust norms as well (especially in the EU)
- GloBE proposals – multiple consequences may ensue if income is not subject to tax at a minimum effective rate (Including income-pick up in parent jurisdiction, denial of deduction and treaty benefits, and levy of withholding tax at source)

# Other factors affecting tax planning

---

- Enactment of General and Special Anti-abuse rules by most countries, including India
- Emergence of “tax morality” – purpose and acceptability of tax outcomes are increasingly relevant
- Tax matters routinely make news headlines – tax planning will need to survive the glare of spotlight
- Increased data leaks - confidentiality and secrecy no longer assured
- Debate over MNCs tax strategies plays out in social media
- Increased interest on the part of media, NGOs and even consumers in tax matters

# Takeaways

# Takeaways - where do we stand today?

---

## 'Tax planning' in the era of BEPS and MLI

**What is 'tax planning'?**

Reduction of tax liability with little or no impact on economic circumstances

Ascertaining and implementing the most tax efficient way of achieving business objectives

**Are all attempts to reduce tax liability restricted post BEPS and MLI?**

# Takeaways - the future of tax planning

---

**Traditional approach to tax planning won't work**

**Planning for real business transactions still possible...but this will be subject to:**

- a) Higher risk of scrutiny**
- b) Higher threshold for 'acceptability'**
- c) Must satisfy larger number of stakeholders**

**Extremely robust documentation and proof of actual conduct critical**



# Takeaways - impact on Professionals

---

- Role of professionals will see a transformation
- Changed expectations from clients - need to manage significantly increased tax risks without overpaying taxes
- Mere compliance with rules insufficient – acceptability and morality are increasingly relevant
- All planning must be geared up to face rigorous (and possibly public) scrutiny
- Mandatory Disclosure Requirements for BOTH – Intermediaries and Taxpayers ?



# Thank you

**#KPMGjosh**



[home.kpmg/in/socialmedia](https://home.kpmg/in/socialmedia)

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

© 2020 KPMG, an Indian Registered Partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. All rights reserved.

The KPMG name and logo are registered trademarks or trademarks of KPMG International.

This document is for e-communication only