GEGAFRICA
GLOBAL ECONOMIC GOVERNANCE

DISCUSSION PAPER | MARCH 2017

FIGHTING BASE EROSION AND PROFIT SHIFTING IN AFRICA

A REVIEW OF COUNTRY-BY-COUNTRY REPORTING

Peter Draper & Heinrich Krogman

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The Global Economic Governance (GEG) Africa programme is a policy research and stakeholder engagement programme aimed at strengthening the influence of African coalitions at global economic governance forums such as the G20, BRICS, World Trade Organization and World Bank, among others, in order to bring about pro-poor policy outcomes.

The second phase of the programme started in March 2016 and will be implemented over a period of three years until March 2019.

The programme is expected to help create an international system of global economic governance that works better for the poor in Africa through:

- undertaking substantial research into critical policy areas and helping South African policymakers to prepare policy papers for the South African government to present at global economic governance platforms;
- ensuring that African views are considered, knowledge is shared and a shared perspective is developed through systematic engagement with African governments, regional organisations, think tanks, academic institutions, business organisations and civil society forums; and
- disseminating and communicating research and policy briefs to a wider audience via mass media and digital channels in order to create an informed and active policy community on the continent.

For the next three years the work of the programme will be focused on three thematic areas: development finance for infrastructure; trade and regional integration; and tax and transparency.

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THEME 2: TAX AND TRANSPARENCY

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ABSTRACT

Multinational enterprises (MNEs) can shift profits away from jurisdictions with comparatively high tax rates to jurisdictions with lower to no tax rates, and thus avoid paying their fair share of taxes without breaking any single jurisdiction's laws. This is in part possible owing to the restricted exchange of information (EOI) between national tax authorities, which limits these authorities' capacity to conduct accurate MNE audits. In response, the Organization for Economic Cooperation and Development (OECD), with support from the G20, drafted the 'OECD/G20 Base Erosion and Profit Shifting (BEPS) Package', a set of 13 reports with 15 action plans. One important aspect in addressing BEPS is to increase the reliability and comparability of tax information between tax jurisdictions. Implementation of Action 13 – 'Transfer pricing documentation and country-by-country reporting (CbCR)' – is seen as part of the solution. By creating a set of standard reporting templates and model legislation to collect an MNE's relevant business information, which could impact its corporate income tax liability, and establishing multilateral agreements to facilitate EOI across jurisdictions between tax authorities, Action 13 takes an important step towards addressing the current tax disclosure and transparency gaps and limiting the extent to which MNEs can shift their taxable profits. However, the proposed set of recommendations has a limited scope and is technically onerous to implement in poor, particularly African, countries where revenue authorities are severely resource-constrained. These issues and dilemmas are reviewed in relation to African resource mobilisation needs, and with an eye to the 2020 review of CbCR implementation.

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GLOSSARY

Base erosion and profit shifting (BEPS)[a]

Base erosion and profit shifting (BEPS) refers to tax planning strategies that exploit gaps and mismatches in tax rules to make profits 'disappear' for tax purposes or to shift profits to locations where there is little or no real activity but the taxes are low, resulting in little or no overall corporate tax being paid.

Aggressive tax planning[b]

Aggressive tax planning refers to a multinational enterprise (MNE) tax structure or scheme that exploits differences between various countries' tax laws to avoid due tax responsibility. It can take the form of **hybrid mismatch arrangements**, meaning arrangements exploiting differences in the tax treatment of instruments, entities or transfers between two or more countries often leading to double non-taxation, double deduction and long-term deferral.

Convention on Mutual Administrative Assistance in Tax Matters (the Convention)[c]

The Convention was developed jointly by the Organization of Economic Cooperation and Development (OECD) and the Council of Europe in 1988 and amended by Protocol in 2010. It is the most comprehensive multilateral instrument available for all forms of tax cooperation to tackle tax evasion and avoidance. The amended Convention facilitates international cooperation on national tax laws, while respecting the fundamental rights of taxpayers. It provides for all possible forms of administrative cooperation between states in the assessment and collection of taxes, in particular with a view to combating tax avoidance and evasion.

Multilateral Competent Authority Agreement on the Exchange of CbC Reports (CbC MCAA)[d]

The Convention, by virtue of its Article 6, requires the competent authorities of the parties to the convention to mutually agree on the scope of the automatic exchange of information (EOI) and the procedure to be complied with. As a result, the Country-by-Country (CbC) Multilateral Competent Authority Agreement (MCAA) was developed to set forth rules and procedures as may be necessary for competent authorities of jurisdictions, implementing BEPS Action 13, to automatically exchange CbC reports prepared by the reporting entity of an MNE group.

a UNECA (UN Economic Commission for Africa), 'Illicit Financial Flow: Report of the High Level Panel on illicit financial flows from Africa', February 2015, http://www.uneca.org/sites/default/files/PublicationFiles/iff_main_report_26feb_en.pdf, accessed 25 August 2016.

b OECD (Organization for Economic Cooperation and Development), 'BEPS: frequently asked questions', http://www.oecd.org/ctp/beps-frequentlyaskedquestions.htm, accessed 25 August 2016.

c OECD, 'Convention on Mutual Administrative Assistance in Tax Matters', http://www.oecd.org/tax/exchange-of-tax-information/convention-on-mutual-administrative-assistance-in-tax-matters.htm, accessed 25 August 2016.

d *Ibid*.

INTRODUCTION

Following the Panama Papers leak and numerous press reports of aggressive tax planning by multinational enterprises (MNEs) around the world, there has been a concerted effort, notably in developed countries, to combat MNE tax avoidance and increase international cooperation in tax matters. As MNEs operate across borders they can use multi-jurisdictional tax planning, in combination with transfer pricing, to limit their tax obligations. A key responsive measure to address aggressive MNE tax planning has been the 'OECD/G20 Base Erosion and Profit Shifting (BEPS) Package'. Its aim is to close loopholes between various national tax authorities that allow MNEs to shift profits across borders and pay less than their fair share of taxes. Within this a key component, and part of the minimum BEPS action requirements called the 'Inclusive Framework', is Action 13 – 'Transfer pricing documentation and country-by-country reporting' (CbCR).

In its current iteration, Action 13 aims to provide a documentation and exchange of information (EOI) standard that revenue authorities can use to better understand MNEs' operational structures and subsequently enhance transfer pricing risk assessments. This information should also assist in identifying where auditing resources should be deployed. Considering the increase in information and transparency, the Action 13 reports could assist revenue authorities to collect taxes from MNEs, which in turn would enhance domestic resource mobilisation (DRM), a key issue that African states struggle with. However, the international tax landscape is a complicated tapestry of standards, agreements, treaties and systems, and to effectively address BEPS African states must engage with the content put forward in the Inclusive Framework on BEPS.

First this paper considers why BEPS was developed and why Action 13 is included in the Inclusive Framework as one of four priority BEPS actions. Second, it considers the current state of Action 13 as reported in the final OECD report and how the action is structured. This section of the paper dissects what Action 13, and specifically CbCR, entails for MNEs and revenue authorities.

Third, it considers how the global community has reacted to the proposed action, particularly African states. As the implementation requirements are high, demanding that states make changes to domestic legislation and adhere to stringent EOI thresholds, it considers the challenges African countries face. The section also includes a focus on the South African reaction as an African state that is committed to fully implementing Action 13, in line with the OECD guidelines.

Finally, it looks at the direction in which the debate might head and the issues that might be included in the 2020 review of Action 13. As the implementation of the action plan is likely to have a great impact on the transparency of MNEs' operational and tax structures and the availability of information on the corporate income taxes they pay, African states must consider what points they want to include in the 2020 review.

INTRODUCING THE PROBLEM: WHY CBCR WAS DEVELOPED

MNEs constantly search for ever-increasing effective and profitable value chains to keep pace with competition. Material and transportation costs, production capacity, quality of products and wages all play a part in determining the structure of an MNE's value chain, while taxation plays a role in the location of operations and associated legal structures. Some MNEs see cross-country differences in tax rates

MNEs that do not pay their taxes, where taxes are due owing to operating realities rather than artificially adjusted tax responsibilities, are avoiding their designated and expected tax contributions to the public sector

as just another component to be considered in structuring their cross-border value chains, while others aggressively plan an operation around tax structures, meaning that they can avoid paying their fair share of tax. The latter is mostly legal, as MNEs generally do not breach any single tax jurisdiction's laws. However, it has a negative impact on the countries in which they are operating, regardless of whether it is legal or not. By avoiding tax MNEs do not contribute their fair share, meaning MNEs that do not pay their taxes, where taxes are due owing to operating realities rather than artificially adjusted tax responsibilities, are avoiding their designated and expected tax contributions to the public sector. This reduces their host nation's tax revenues, thus undermining the provision of public services used by all citizens in the host country, including MNEs. Furthermore, MNEs that operate across borders can use tax planning to gain a competitive advantage over enterprises that operate at a domestic level.

According to the OECD, an estimated 4% to 10% (or $100–240 billion) of global corporate income tax (CIT) revenue is lost every year because of the activities described, constituting what has become known as BEPS. In the last few years, the most notable companies accused in the media[1] of avoiding taxes have been Amazon, Starbucks and Google, operating in the UK, and Apple, operating in Ireland. As developed countries, particularly, have gone through austerity programmes imposed by their respective governments to balance their finances in the wake of the 2008–09 global financial crisis, the idea that various MNEs pay little or no corporate tax has drawn considerable public rebuke and seen a growing sentiment to increase tax collection efficiency and disclosure.

While the principle of addressing BEPS received broad-based support in the G20, it also encountered resistance in some developed countries, which remain concerned that it could be used to unfairly single out their MNEs as targets for enhanced revenue collection

In response, the OECD and the G20 developed the 'OECD/G20 Base Erosion and Profit Shifting (BEPS) Package'. This includes a list of 15 action plans containing model legislation, multilateral agreements and implementation guidelines, and aims to develop a global response to the tax administration issues associated with BEPS. While thought of as a developed country agenda, it is worth remembering that while developed countries brought the BEPS agenda to the OECD, and the OECD brought it to the G20, in the G20 the agenda received support from developing countries too, as they host MNEs themselves and are concerned with increasing their own tax revenues. While the principle of addressing BEPS received broad-based support in the G20, it also encountered resistance in some developed countries, which remain concerned that it could be used to unfairly single out their MNEs as targets for enhanced revenue collection. These countries are also concerned about issues

1 *Bloomberg News*, 'Google revenues sheltered in no-tax Bermuda soar to $10 billion', 10 December 2012, Billionhttp://www.bloomberg.com/news/articles/2012-12-10/google-revenues-sheltered-in-no-tax-bermuda-soar-to-10-billion, accessed 25 August 2016; *BBC*, 'Google, Amazon, Starbucks: The rise of "tax shaming"', 21 May 2013, http://www.bbc.com/news/magazine-20560359, accessed 25 August 2016; *Fortune*, '7 corporate giants accused of evading billions in taxes', 11 March 2016, http://fortune.com/2016/03/11/apple-google-taxes-eu/ accessed 25 August 2016.

around the confidentiality of taxpayer information. Furthermore, while the OECD cites the importance of the BEPS package for developing countries, 'given their reliance on corporate income tax',[2] it is not clear how effective the approach would be to increase DRM in African states, particularly as it relates to CbCR. This complex political economy inevitably constrained what could be achieved through the G20 in relation to BEPS, and CbCR in particular.

Developing countries' priority actions in BEPS

In 2014, following a recognition that the manifestation of BEPS varies in developed and developing countries, the UN Committee of Experts on International Co-operation in Tax Matters (UN Tax Committee) began a process of soliciting developing countries' views on 'fair and appropriate means of responding to the challenges imposed by base erosion and profit shifting'.[3] This was done through a questionnaire that gauged which of the 15 actions in the BEPS Action Plan were a priority for developing countries. It also helped identify obstacles to implementing the BEPS Action Plan. Thirteen countries responded and were willing to have their responses made public. Of these, three were African, namely Ghana, Lesotho and Zambia. Non-governmental organisations (NGOs) that responded were Christian Aid, ActionAid, Economic Justice Network and Oxfam South Africa.[4]

In response to the question 'If you are affected by base erosion and profit shifting, what are the most common practices or structures used in your country or region, and the responses to them?', respondents overwhelmingly identified transfer pricing as the most significant reason for base erosion and profit shifting.[5] This correlates to the responses given to the question 'Which of these OECD action points do you see as being most important for your country, and do you see that priority changing over time?' (see Figure 1). Respondents overwhelmingly listed actions 8 ('Assure that transfer pricing outcomes are in line with value creation: Intangibles'), 9 ('Assure transfer pricing outcomes are in line with value creation: Risk and capital)', 10 ('Assure that transfer pricing outcomes are in line with value creation with reference to other high-risk transactions, in particular, management fees') and 13 ('Re-examine transfer pricing documentation') as top priorities for them.

Our report focuses on Action 13, which specifically addresses transfer pricing documentation. It requires countries to amend their domestic tax legislation, effectively placing an additional reporting burden on MNEs by requiring additional

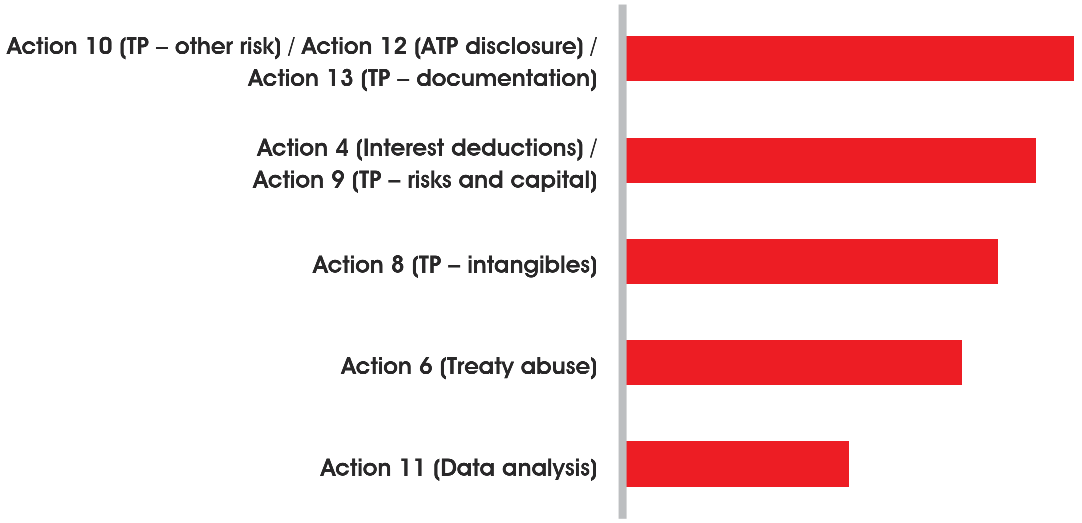
2 OECD, 'Part 1 of a Report to G20 Development Working Group on the Impact of BEPS in Low Income Countries', 13 August 2014a, http://www.oecd.org/tax/part-1-of-report-to-g20-dwg-on-the-impact-of-beps-in-low-income-countries.pdf, accessed 27 August 2016.

3 Peters C, *Bulletin for International Taxation*, June/July 2015, p. 375.

4 *Ibid.*, p. 375.

5 *Ibid.*, p. 377.

FIGURE 1 ORDER OF PRIORITY OF BEPS ACTIONS



Source: Peters C, *Bulletin for International Taxation*, June/July 2015, p. 379

tax reporting to the tax authorities[6] in whose jurisdiction they operate, as well as requiring countries to sign multilateral/bilateral EOI agreements, thus demanding that states comply with new tax information disclosure and EOI requirements. The EOI agreements are required to guarantee the confidentiality of MNEs' disclosed tax information, thereby reassuring other member states, notably developed states, that their MNEs will not be targeted as 'cash cows' for enhanced tax investigations.

In its current form CbCR has a narrow focus on reporting and disclosing MNEs' income/revenue tax, as well as information on capital and number of employees. This information, when considered in conjunction with the remaining reporting tiers of Action 13, might increase CIT transparency and availability of information, and thereby assist in identifying MNEs that might be abusing transfer pricing. The reports could be used to conduct better-targeted risk assessments which, in turn, could result in increased corporate income tax collections. Of course, much depends on the use to which participating revenue authorities put the ensuing information, a point to which we return below.

6 Under Action 13 MNEs are required to record, report and file three additional tax reports, discussed in more detail in the 'Structure of Action 13' subsection, in addition to other tax administrative requirements.

To determine whether CbCR can deliver on its intended outcomes for African countries, it is first necessary to understand the BEPS and CbCR agenda and requirements.

BASE EROSION AND PROFIT SHIFTING

The OECD report 'Addressing Base Erosion and Profit Shifting' found that current global tax rules provide opportunities to shift profits via legal constructs, and to shift around the risks within an MNE group, thereby reducing the share of profits associated with revenue- and profit-generating activities out of countries where taxes should be paid on these economic activities. Table 1 lists the OECD/G20 15-point Action Plan that aims to address the problems enabling BEPS.

TABLE 1 OECD/G20 BEPS PACKAGE

REPORT	ACTION PLAN
Addressing the tax challenges of the digital economy	Action 1: Digital economy
Neutralising the effects of hybrid mismatch arrangements	Action 2: Hybrids
Designing effective controlled foreign company (CFC) rules	Action 3: CFC rules
Limiting base erosion involving interest deductions and other financial payments	Action 4: Interest deductions
Countering harmful tax practices more effectively, taking into account transparency and substance	Action 5: Harmful tax practices
Preventing the granting of treaty benefits in inappropriate circumstances	Action 6: Treaty abuse
Preventing the artificial avoidance of permanent establishment status	Action 7: Permanent establishment status
Aligning transfer pricing outcomes with value creation	Actions 8: Transfer pricing, intangibles
	Actions 9: Transfer pricing, risks & capital
	Actions 10: Transfer pricing, high-risk transactions
Measuring and monitoring BEPS	Action 11: BEPS data analysis
Mandatory disclosure rules	Action 12: Disclosure of aggressive tax planning
Transfer pricing documentation and CbCR	Action 13: Transfer pricing documentation
Making dispute resolution mechanisms more effective	Action 14: Dispute resolution
Developing a multilateral instrument to modify bilateral tax treaties	Action 15: Multilateral instrument

Source: OECD, 'BEPS actions', http://www.oecd.org/tax/beps/beps-actions.htm, 2016

The core of this agenda revolves around minimising the opportunities for MNEs to use aggressive tax planning, within which transparency in reporting where profits are earned across national jurisdictions is the most effective antidote, given the current limitations to international tax cooperation. Furthermore, it is worth noting that the broader conversation within which the BEPS package falls revolves around increasing the effectiveness of tax collection by revenue authorities, where ineffectiveness is mainly caused by a lack of information. As noted by Oxfam, 'In our view, the ultimate goal of such reporting is to improve tax governance, accountability and transparency for both companies and governments in developed and developing countries.'[7]

Currently one of the main issues is the inability of tax authorities to assess transfer pricing abuse, as information is not readily available or directly comparable. To understand why transfer pricing is such a vital component in the BEPS package, a brief discussion on transfer pricing and the arm's-length principle is necessary.

Transfer pricing, base erosion and the arm's-length principle

Transfer pricing is the setting of prices for tangible and intangible goods and services sold between controlled or related legal entities within a group of related companies. While transfer pricing is not illegal, and is often a necessary part of conducting business, the issue is transfer mispricing. Specifically, by adjusting transfer prices MNEs can move their taxable profits away from high tax jurisdictions to lower or non-tax jurisdictions. According to Reuters UK, Starbucks 'transferred money to a Dutch sister company in royalty payments, bought coffee beans from Switzerland and paid high interest rates to borrow from other parts of the business'.[8] In this scenario Starbucks, the MNE, records low or no profits in the country it is selling its coffee, but its income in that country is artificially eroded by high inter-enterprise and, in this case, cross-border costs. The difficulty in determining the arm's-length value of intangibles, in this example the value of the Starbucks brand and related royalty value, further complicates the assessment of transfer mispricing.

Under the arm's-length principle, it is assumed that an MNE's operations, in their various jurisdictions, would naturally want to be competitive in their respective markets; and that the parties to a transaction, even an inter-enterprise transaction, are independent and on an equal footing. However, as MNEs operate across borders the gains from avoiding tax in one jurisdiction can compensate for uncompetitive business practices in another, thereby increasing the incentive to engage in transfer mispricing.

7 OECD, 'Discussion Draft on Transfer Pricing Documentation and CbC Reporting: Public Comments Received Volume III - Letters K to R', 23 February 2014, http://www.oecd.org/ctp/transfer-pricing/volume3.pdf, accessed 14 October 2016.

8 *Reuters*, 'Special Report - How Starbucks avoids UK taxes', 15 October 2012, http://uk.reuters.com/article/uk-britain-starbucks-tax-idUKBRE89E0EW20121015, accessed 25 August 2016.

Arm's-length transactions are specifically used in commercial deals to arrange an equitable agreement that will stand up to legal scrutiny even though the parties may have shared interests. Tax legislation and OECD guidelines have attempted to give proper substance to this arm's-length concept, which has caused all the real issues in transfer pricing and tax disputes. BEPS is trying to refine the concept. But documentary compliance and the associated audits, as they relate to establishing whether transactions occurred at arm's-length, can be burdensome and costly. They might also ultimately prove ineffective, given the complexity of audits across multiple tax jurisdictions and the complexities of determining arm's-length terms and conditions.

Chapter V of the Transfer Pricing Guidelines on Documentation provides guidance to assist taxpayers in identifying documentation that would be helpful in showing that their transactions satisfy the arm's-length principle. This chapter also notes that,[9]

> [b]y requiring taxpayers to articulate convincing, consistent and cogent transfer pricing positions, transfer pricing documentation can help to ensure that a culture of compliance is created. Well-prepared documentation will give tax administrations some assurance that the taxpayer has analysed the positions it reports on tax returns, has considered the available comparable data, and has reached consistent transfer pricing positions.

Standardised documentary compliance is considered necessary to achieve a more transparent global tax environment, ultimately assisting tax jurisdictions to increase tax collection and, where need be, perform audits and reduce taxpayers' compliance burden through having a more standardised approach. This increase in transparency via standard documentary compliance with EOI between tax jurisdictions is the main focus of Action 13 of the BEPS package.

Transfer pricing documentation and CbCR

As the name suggests, Action 13, 'Transfer pricing documentation and country-by-country reporting', focuses on enhancing the transparency of MNEs' tax structures as they relate to transfer pricing and related tax risk assessment, by allocating roles and responsibilities to specific MNE entities. It contains revised standards on transfer pricing documentation, including the template for CbCR. It is thought that these revised standards will increase transparency, as they require taxpayers to articulate consistent transfer pricing positions and provide tax administrations with useful information to assess transfer pricing risks, which in turn can be used to determine where audit resources can most effectively be deployed. The CbCR template, with associated EOI agreements, is thought to be the appropriate tool for EOI, gathered via the revised reporting standards, between tax authorities.

9 OECD, 'Transfer Pricing Documentation and Country-by-Country Reporting ACTION 13: 2015 Final Report, Chapter V of the Transfer Pricing Guidelines on Documentation', 2015.

What does BEPS and CbCR aim to achieve?

Enduring, long-term solutions would rest on institutional reforms, well-managed global coordination and effective engagement between governments and business groups to ensure a meaningful international effort to address tax avoidance. It is thought that the BEPS package will benefit all states regardless of their level of development; however, given the wide scope of the BEPS package a list of priority issues needs to be considered to contextualise the relative importance of the CbCR agenda.

Through consultations with developing country governments and NGOs, the OECD report[10] on the impact of BEPS in low-income countries found the following to be priority issues:

- excessive or unwarranted payments to MNE affiliates – eroding the tax base;
- challenges stemming from new models for doing business, such as highly fragmented global value chains;
- developing countries' struggle to obtain the information they need to assess and address BEPS issues; and
- the acute pressure developing countries face to attract investment by offering tax incentives, which may erode the country's tax base with little demonstrable benefit.

While the list of priority issues touches several BEPS actions, the third point relates directly to the current lack of information, and the comparability of said information, to assess the transfer pricing risks that Action 13 is attempting to address. One proposed solution to transfer pricing abuse, among the four included in the OECD BEPS actions, is to increase the tax transparency of MNEs by requiring that national tax authorities implement Action 13. The implementation package for Action 13 consists of model legislation as well as implementation arrangements for the automatic exchange of CbC reports. It is thought that this pre-emptive agreement on the implementation package and its subsequent structure should cut down on negotiation time for participating members and future members.

Structure of Action 13

A three-tiered standardised approach to transfer pricing documentation has been developed. First, the guidance on transfer pricing documentation requires MNEs' headquarters to provide tax administrations in which they are resident with a 'Master file', which should contain high-level information regarding their global business operations and transfer pricing policies. The Master file is to be available

10 OECD, 'Part 2 of Report to G20 Development Working Group on the Impact of BEPS in Low Income Countries', 13 August 2014b, https://www.oecd.org/g20/topics/taxation/part-2-of-report-to-g20-dwg-on-the-impact-of-beps-in-low-income-countries.pdf, accessed 19 August 2016.

to all 'relevant' tax administrations in those countries party to BEPS Action 13 in which the MNE operates. Second, it requires that detailed transactional transfer pricing documentation be provided in a 'Local file' specific to each country in which the MNE operates, by the MNE's subsidiaries based in the country concerned. Third, MNE groups with revenues of more than EUR[11] 750 million ($850 million) per year in the preceding fiscal year are required to file a CbC report that will provide annually via automatic exchanges, and for each tax jurisdiction in which they do business, the amount of revenue, profit before corporate income tax, and corporate income tax paid and accrued.

CbCR template requirements and issues

The templates for the CbC reports, as per the OECD's 'Transfer Pricing Documentation and Country-By-Country Reporting, Action 13 2015 Final Report', are shown in the Appendix. CbCR requires MNE groups with revenues of more than EUR 750 million to report:

- the amount of revenue;
- profit before income tax;
- income tax paid and accrued;
- number of employees;
- stated capital;
- retained earnings; and
- tangible assets in each tax jurisdiction.

The template 'List of All the Constituent Entities of the MNE Group Included in Each Aggregation per Tax Jurisdiction'[12] requires qualifying MNEs (based on the annual consolidated group revenue threshold) to disclose:

- the tax jurisdiction;
- constituent entities resident in the tax jurisdiction;
- the tax jurisdiction of organisation or incorporation, if different from the tax jurisdiction of residence; and
- main business activity(ies),

where 'constituent entities' means:[13]

i 'any separate business unit of an MNE group that is included in the Consolidated Financial Statements of the MNE group for financial reporting purposes, or

11 Currency code for the EU euro.

12 See Appendix.

13 OECD, 'Action 13: Country-by-Country Reporting Implementation Package', https://www.oecd.org/ctp/transfer-pricing/beps-action-13-country-by-country-reporting-implementation-package.pdf, accessed 25 August 2016.

would be so included if equity interests in such business unit of the MNE group were traded on a public securities exchange,

ii 'any such business unit that is excluded from the MNE group's Consolidated Financial Statements solely on size or materiality grounds,

iii 'any permanent establishment of any separate business unit of the MNE group included in (i) or (ii) above provided the business unit prepares a separate financial statement for such permanent establishment for financial reporting, regulatory, tax reporting, or internal management control purposes.'

The requirements from this template should provide more information on a qualifying MNE's activities and resultant CIT obligations. For some MNEs this information is available, but the feedback from MNEs is that it is not readily available at the country level, as required by the CbCR template. This level of information is not available since other stakeholders (eg, those requiring annual financial statements, integrated reports, etc.) do not currently request that it be presented in this granular format, and so it is generally not generated by MNEs. Nonetheless, demands for full disclosure of CbCR data at all levels are growing. For this reason, but also because the official CbCR template requires it, MNEs must put data collection processes in place to comply.

Implementing these reforms to address aggressive tax planning (as it relates to transfer pricing) and increase tax transparency (via CbCR) is complex at the national level. This is because current reporting standards and diverging interests can slow down the process or make changes to national legislation to such an extent that it is no longer consistent with the OECD's proposed standards. Local file reporting requirements are only submitted to the national tax authority, giving it considerable design flexibility relative to the more demanding CbCR requirements. Australia, for example, has released its final design of the Local file, as part of its implementation of CbCR requirements. Owing to an overlap in existing transfer pricing reporting requirements its Local file has two tiers: a 'short-form Local file'[14] and a 'Local file'.[15] Since its two-tier format is not the same as the OECD's proposed Local file, MNEs will have to pay specific attention to the unique Australian Local file and transfer pricing requirements when implementing their global CbCR strategy.

Implementation of CbCR requirements

The OECD's final report on 'Transfer Pricing Documentation and Country-By-Country Reporting' provides detailed guidelines on the implementation of Action 13, taking account of the fact that its success depends on the extent of implementation globally. It recommends that the first CbC reports be filed for MNE fiscal years beginning on or after 1 January 2016. It also stipulates the underpinning conditions for tax authorities sharing CbC reports with other tax authorities, and

14 For MNEs with sufficiently small and/or low-risk internationally related party dealings.

15 For all other affected taxpayers.

expands on the confidentiality of taxpayer information, consistency in reports, and the appropriate use of CbC reports.

Sharing of information

As part of the implementation package for the government-to-government exchange of CbC reports the OECD developed model legislation requiring the ultimate parent entity of an MNE group to file the CbC report in its jurisdiction of residence, and implementation arrangements for the automatic exchange of CbC reports under international agreements. Countries are required to have signed, or have expressed their intention to sign, the Convention on Mutual Administrative Assistance in Tax Matters (the Convention, or the Convention amended by Protocol) and acknowledge that the Convention must be in force and in effect in relation to them before the automatic exchange of CbC reports can take place between tax authorities. Such information exchanges will be secured through countries' ratifying the CbC MCAA, or through bilateral agreements such as double taxation treaties or tax information exchange agreements (TIEAs).

States are obligated to keep information confidential and to complete a questionnaire on tax information confidentiality to become party to the Convention. The questionnaire requires states to explain how their domestic legislation, rules, regulations, administrative procedures and practices ensure the confidentiality of information exchanged for tax purposes; focusing on confidentiality of exchanged information safeguards, exceptions permitting disclosure of exchanged information, confidentiality of communications between the competent authorities, and provisions for penalties for breach of confidentiality. This is to give assurance to members that their taxpayer information will be treated with due care and confidentiality by other participating members.

Common reporting standards

To facilitate the international comparability of tax information, Section 3 of the CbC MCAA requires that the currency of the amounts contained in the CbC report be specified, that CbC report exchanges occur within a reasonable and predictable timeframe, that CbC reports be exchanged via a common schema in Extensible Markup Language (CbCR XML schema), and that the competent authorities will work towards and agree on one or more methods for electronic data transmission, including encryption standards.

However as noted in the previous section, some revenue authorities in developing countries might face capacity constraints in adopting the CbCR XML schema, especially the related information technology (IT) requirements. In this regard the EOI requirements might prove difficult to adhere to in countries with low information and communications technology (ICT) absorption and use, especially in those countries where tax returns are still filed manually. Globally, 49 states have signed the CbCR MCAA, requiring the use of the CbCR XML schema for the exchange of CbC reports, of which only three are from the African continent: Nigeria, Senegal and South Africa.

The EOI requirements might prove difficult to adhere to in countries with low information and communications technology absorption and use, especially in those countries where tax returns are still filed manually

In states where tax returns are still filed manually, the administrative and ICT infrastructure requirements constitute a serious constraint. Fortunately, the G20's Development Working Group (DWG) is working on eight toolkits to assist low-capacity developing countries to implement the four minimum standards. In addition, the OECD and the Global Forum have identified several initiatives to address the top priority BEPS issues identified by developing countries. However, the IT initiative is yet to be released.

Appropriate use and limitations of CbC reports

In terms of appropriate use of CbC reports, the implementation guidelines acknowledge that CbCR has a very focused purpose. CbC reports' ultimate purpose is for tax authorities to share information among themselves to assist with identifying potential transfer pricing abuse within an MNE. Ultimately, the information received by means of the CbC reports should be used to do an initial transfer pricing and BEPS risk assessment and, where appropriate, for economic and statistical analysis (ie, to see in effect if there is any obvious transfer pricing and profit shifting abuse). As mentioned in Section 5 of the CbC MCAA, 'Country-by-Country Reports should not be used as a substitute for a detailed transfer pricing analysis of individual transactions and prices based on a full functional analysis[16] and a full comparability analysis[17]. CbC reports are not meant to be used as a shortcut to a tax audit – an outcome that certain developed countries were apparently keen to secure.[18]

16 A functional analysis should provide an overview of the organisation, seek to identify the functions performed, assets held and risks borne by each operation of the group and assess the importance of each function to the overall operations of the group. A functional analysis is necessary in determining whether or not controlled and uncontrolled transactions or entities are comparable.

17 The concept of comparability analysis is used in the selection of the most appropriate transfer pricing method as well as in arriving at the correct arm's-length prices or profits or financial indicators. OECD, 'Action 13: Guidance on the Implementation of Transfer Pricing Documentation and Country-by-Country Reporting', 2015, https://www.oecd.org/ctp/beps-action-13-guidance-implementation-tp-documentation-cbc-reporting.pdf, accessed 19 August 2016.

18 Interview with a revenue administration official.

REACTIONS TO ACTION 13

The information available via the CbCR process, in principle, could be of use to developing country tax authorities in potentially increasing CIT collection, and could ensure audits of MNEs are more focused and effective in using local resources. However, there is also the potential that CbCR, or the related Master and Local file reporting, could increase the amount of transfer pricing audits required by developing countries, putting additional strain on already stretched tax authority resources. This will increase the premium on prioritisation of cases, which in turn requires commensurate internal capacity in the revenue authority in question which, in the African context, brings the opportunity cost issues into sharper focus. On the other hand, at least the universe of potentially problematic taxpayers will be more clearly known. Only time will tell whether developing countries' tax authorities will find the information useful to address these concerns.

African challenges

The African Tax Administration Forum (ATAF) notes that African countries face challenges in exchanging information related to tax matters owing to insufficient legal instruments, insufficient domestic legislation, inadequate policies, processes and procedures, and lack of skilled staff to manage and process the EOI requests.

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Therefore, ATAF and the Global Forum have developed a three-year programme focusing on tax transparency and EOI in Africa, called the Africa Initiative. ATAF also created its own three-year EOI programme, working on BEPS with the G20 DWG – responsible for a report on the main sources of BEPS in developing countries and how these relate to the OECD/G20 BEPS Action Plan on these issues – and seeking to establish competent authority offices in all ATAF member states.[19] Unfortunately, the EOI challenges identified by ATAF can be persistent in the absence of the political will to adopt change.

19 ATAF members: Benin, Botswana, Burkina Faso, Burundi, Cameroon, Chad, Comoros, Côte D'Ivoire, Egypt, Eritrea, Gabon, Gambia, Ghana, Kenya, Lesotho, Liberia, Madagascar, Malawi, Mauritania, Mauritius, Morocco, Mozambique, Namibia, Niger, Nigeria, Rwanda, Senegal, Seychelles, Sierra Leone, South Africa, Sudan, Swaziland, Tanzania, Uganda, Zambia, Zimbabwe.

Furthermore, in the African context related but different concerns are currently occupying policymakers' attention, as noted by the list of action plans considered to be of high importance in addressing priority issues in developing states (see previous section).[20]

To illustrate the point of CbCR implementation priority for African states, Table 2 shows the commitments African states have made toward fully implementing CbCR and the related agreements on EOI. Of the 12 African states that have shown interest in or commitment to the Convention, only three have signed the CbC MCAA. This means that if states that are not party to the CbC MCAA or listed as a non-reciprocal jurisdiction receive CbC reports from MNEs resident in their jurisdiction, they will not share the information with other tax authorities; nor can they receive these pursuant to a bilateral EOI agreement. For CbCR to be effective it is vital that more than three African countries commit to the CbCR MCAA, but given the concerns raised regarding the implementation of CbCR requirements African states seem hesitant to commit. In this regard it is important that African states receive the required assistance to implement and comply with the MCAA requirements, which depends on the eight toolkits being developed by the DWG and the proposed assistance initiative from the OECD and the Global Forum.

The problem is that there are divergent emphases placed on the importance of each of the 15 action plans in the BEPS package for the main countries involved in these debates. Developed countries have the official development assistance resources to assist the poorest African countries combat these BEPS problems, while African countries themselves face significant opportunity costs and the potential threat of foreign direct investment diversion, should they adopt rigorous compliance approaches to combating these tax problems, since that may negatively shift MNEs' risk/reward calculus.

What do African countries really need?

While some African states struggle with DRM, the increased information flow from the proposed Action 13 could provide them with the means to better target risk assessments and consequently increase CIT collection. Considering that some African states heavily depend on CIT revenue from MNEs a strong case can be made for the rapid, widespread implementation of Action 13 on the continent. However, the solution is not that simple. As noted previously, African states struggle with transfer mispricing relating to four BEPS action plans, not just Action 13. Nonetheless, in the following section the specific constraints African countries face with regard to implementing Action 13 are discerned.

20 OECD, 13 August 2014b, *op. cit.*

TABLE 2 SUMMARY OF AFRICAN STATES' COMMITMENT TO IMPLEMENTING CBCR

COUNTRY	CONVENTION ON MUTUAL ADMINISTRATIVE ASSISTANCE IN TAX MATTERS[a] (AMENDED PROTOCOL)	MULTILATERAL COMPETENT AUTHORITY AGREEMENT ON THE EXCHANGE OF COUNTRY-BY-COUNTRY REPORTS
Cameroon	Entry into force 2015	–
Gabon	Signed 2014	–
Ghana	Entry into force 2013	–
Kenya	Signed 2016	–
Mauritius	Entry into force 2015	–
Morocco	Signed 2013	–
Nigeria	Entry into force 2015	Signed
Senegal	Signed 2016	Signed
Seychelles	Entry into force 2015	–
South Africa	Entry into force 2014	Signed
Tunisia	Entry into force 2014	–
Uganda	Entry into force 2016	–

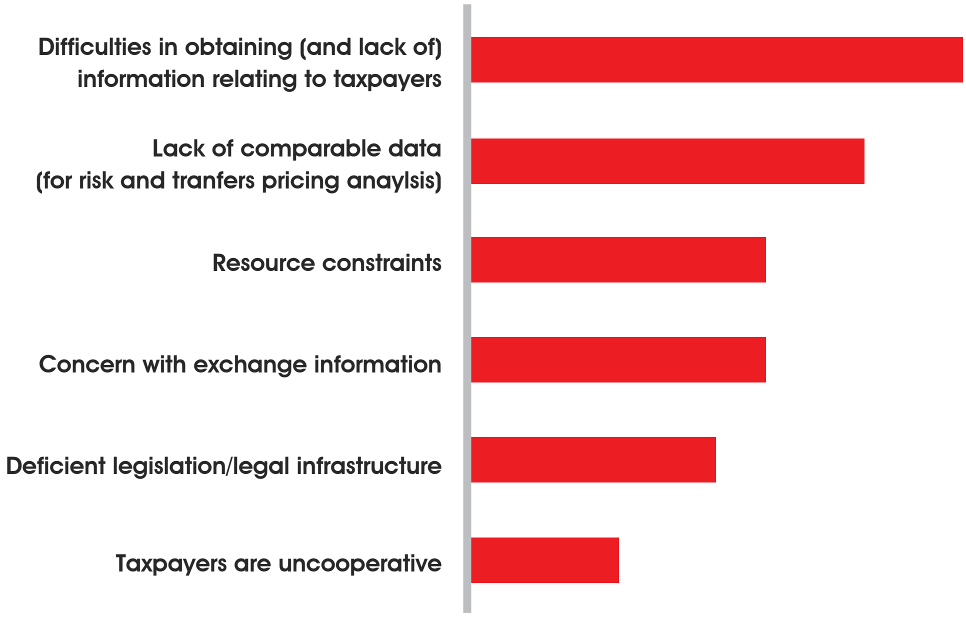
a In the context of the Common Reporting Standard, this requirement has been translated into a Multilateral Competent Authority Agreement

Source: OECD, 'Signatories of the Multilateral Competent Authority Agreement on the Exchange of Country-By-Country Reports (CBC MCAA) and Signing Dates', https://www.oecd.org/tax/automatic-exchange/about-automatic-exchange/CbC-MCAA-Signatories.pdf, accessed 25 August 2016; OECD, 'Jurisdictions participating in the Convention on Mutual Administrative Assistance in Tax Matters Status – 29 July 2016', http://www.oecd.org/tax/exchange-of-tax-information/Status_of_convention.pdf, accessed 25 August 2016

Addressing African capacity constraints in CbCR

Having identified which action points are priority to them in the UN Tax Committee Study, developing countries were asked to identify key constraints to determining the accurate reporting of profits by MNEs. When answering the question 'What main obstacles have you encountered in assessing whether the appropriate amount of profit is reported in your jurisdiction and in ensuring that tax is paid on such profit?', the response can be categorised into two main constraints: access to information (difficulties in obtaining information relating to taxpayers; lack of comparable data; concerns with EOI; uncooperative taxpayers) and capacity to process information (resource constraints; deficient legislation/legal infrastructure).[21] Figure 2 captures the main constraints. Several countries reiterated that they lacked adequate capacity to implement the action plan.

FIGURE 2 OBSTACLES TO DETERMINING WHETHER THE APPROPRIATE PROFITS HAVE BEEN REPORTED



Source: Peters C, *Bulletin for International Taxation*, June/July 2015, p. 378

Accessibility of information: Could technology provide the solution?

The OECD/G20 guidelines for CbCR implementation are underpinned by three fundamental conditions: confidentiality, consistency and appropriate use.[22] While the reasons for each condition are clear, there are concerns that the same conditions are likely to make it difficult for several developing countries, especially

21 Peters C, *op. cit.*, pp. 375, 380.

22 OECD/G20 Base Erosion and Profit Shifting Project, 'Action 13: Guidance on the Implementation of Transfer Pricing Documentation and Country-by-Country Reporting', 2015, p. 5, http://www.oecd.org/ctp/beps-action-13-guidance-implementation-tp-documentation-cbc-reporting.pdf, accessed 20 February 2017.

in Africa, to access information. This is owing to most African tax authorities' capacity constraints, which would make it difficult to set up the requisite technical infrastructure for meeting all the data handling requirements.[23]

The report by the Platform for Collaboration on Tax to the G20 titled 'Enhancing the Effectiveness of External Support in Building Tax Capacity in Developing Countries' calls for development partners to increase their support for managerial and technical skills in taxation agencies.[24] In response, the Global Tax Policy Center (GTPC) at the Vienna University of Economics and Business convened a multi-stakeholder group with the main goal of reducing capacity constraints by using advanced technology to ensure secure management of CbC data.[25] This has resulted in the development of an application known as the Tax Information Exchange (TIE), which is currently being piloted by the Mexico Tax Administration. The aim of the project is to use advanced technology to create a 'simple means of enabling appropriate access to the common transmission system through which treaty exchanged tax information will flow', thus allowing more countries to access country-by-country reports at low or no cost.[26] The application is developed by the GTPC's technology sub-team, which includes Accenture, IBM and Vertex as anchor participants.[27]

A key distinction between this platform and the OECD's Common Transmission Mechanism (CTM) is that the CTM is meant to transfer data from one competent authority to another, while TIE will be used by competent authorities to store and access data. It is worth noting that customs authorities have a similar system for collecting and storing trade statistics, known as the Automated System for Customs Data. At a domestic level, the US uses a third-party contractor (3PC) for collecting tax data.

While the use of technology might make the information more accessible, various legal issues need to be clarified before countries can be satisfied that it meets the standards of data confidentiality and security. The sub-team has conducted a preliminary review of the legal issues around a 3PC to receive and hold CbC data as an agent of the competent authority of a country under the terms of the relevant

23 Vienna WU (Vienna University of Economics and Business), Institute for Austrian and International Tax Law, GTPC (Global Tax Policy Center), 'Memorandum of Understanding Concerning a Pilot Country by Country "System" for Tax Administrations', unpublished document.

24 OECD, 'Enhancing the Effectiveness of External Support in Building Tax Capacity in Developing Countries', p. 4, http://www.oecd.org/tax/enhancing-the-effectiveness-of-external-support-in-building-tax-capacity-in-developing-countries.pdf, accessed 20 February 2017.

25 GTPC, 'Tax Information Exchange Application Demo Introduction', p. 1.

26 *Ibid.*

27 Vienna WU, Institute for Austrian and International Tax Law, GTPC, 'Newsletter 1', unpublished document, p. 1.

double taxation agreements, tax information exchange agreements and the MCAA.[28] Although the sub-team is currently undertaking a more detailed examination of domestic legislation using various case studies, the review of international legal questions and generic treaty law has indicated that there are no obstacles to using a 3PC.[29] However, our interviews with relevant South African authorities and ATAF indicated that the handling of taxpayer information by 3PCs is an uncomfortable concept. Not only are domestic taxpayers likely to find it unappealing, but other revenue authorities might also reconsider their standing EOI agreements with the country in question.

Legal issues to consider on using technology for CbCR

The main issue that needs to be determined is who can access the data once it has been collected and stored. Section 5(1) of the CbC MCAA and Article 22 of the Convention provide guidance on this question.

Section 5(1) of the MCAA draws its confidentiality rules and safeguards from the Convention. It states that 'all information exchanged is subject to the confidentiality rules and other safeguards provided for in the Convention, including the provisions limiting the use of the information exchanged'.[30] The discussion on secrecy is captured under Article 22 of the Convention. Article 22(1) provides guidance on which legislation must govern EOI. It states that the receiving state must apply the same levels of secrecy that are contained in its domestic legislation, while the supplying state may specify other requirements that it deems necessary.

Article 22(2) focuses on who may access and use the information, and for what purpose it may be used. It states that[31]

> such information shall in any case be disclosed only to persons or authorities (including courts and administrative or supervisory bodies) concerned with the assessment, collection or recovery of, the enforcement or prosecution in respect of, or the determination of appeals in relation to, taxes of that Party, or the oversight of the above. Only the persons or authorities mentioned above may use the information and then only for such purposes. They may, notwithstanding the provisions of paragraph 1, disclose it in public court proceedings or in judicial decisions relating to such taxes.

28 Vienna WU, Institute for Austrian and International Tax Law, GTPC, 'Managing Country-by-Country (CbyC) Reports by means of an Independent 3rd Party Contractor (3PC) – The Legal Issues', unpublished document, pp. 1–2.

29 Vienna WU, Institute for Austrian and International Tax Law, GTPC, 'Newsletter 1', *op. cit.*, p. 1.

30 OECD & Council of Europe, 'The Multilateral Convention on Mutual Administrative Assistance in Tax Matters: Amended by the 2010 Protocol', 2011, p. 21, http://www.keepeek.com/Digital-Asset-Management/oecd/taxation/the-multilateral-convention-on-mutual-administrative-assistance-in-tax-matters_9789264115606-en#.WEecO4VOKZ8#page23, accessed 20 February 2017.

31 *Ibid.*, p. 23.

As the GTPC sub-team has observed, Article 22(2)'s limitations on disclosure do not preclude data being stored by a third party. The system can be designed to only store data while restricting access to that data to approved tax authorities, which means disclosure would be restricted to the tax authorities. The OECD has also developed a Confidentiality Guide, which states that '[c]onsultants, service providers, contractors and others having access to confidential tax information should also be subject to background checks/security screening and be contractually bound by the same obligations as employees with respect to confidentiality of tax information'.[32] This would be applicable in the case of a third party managing the application. The GTPC's plan is that once it has piloted the TIE application in enough countries to be satisfied that it meets all the security and operational requirements, it will hand over the application to be owned by an international organisation.

The receiving state must apply the same levels of secrecy that are contained in its domestic legislation, while the supplying state may specify other requirements that it deems necessary

Limitations of the technology platform for Africa: Legislative and human capacity

The first area of limitation is that the technology can only be accessed once the receiving country has satisfied the supplying country that its domestic laws adequately comply with the secrecy provisions in the MCAA. While the CTS offers the possibility of a common reporting system that would make transfer pricing data available to more countries, it has yet to address the constraints of ensuring that African countries' domestic legislation is adequately tailored to promote data security. As seen above, information received under the provisions of a tax treaty must be treated as secret in the same manner as information obtained under the domestic laws of the receiving state. The development of legislation is thus an area in which African tax authorities require assistance. This goes beyond the remit of tax authorities towards capacitating justice departments or any similar authorities tasked with developing secrecy laws that are of an international standard. International institutions such as the World Bank, International Monetary Fund (IMF) and OECD need to think beyond involving their tax units in capacity-building interventions.

The second limitation relates to whether African tax authorities can effectively use the data for the intended purpose, once received. ATAF has found that African countries' limitations vis-à-vis fully understanding the impact of transfer pricing are caused by the 'technicality and difficulty of auditing a multinational firm' as

32 OECD, 'Keeping it Safe: The OECD Guide on the Protection of Confidentiality of Information Exchanged for Tax Purposes', 2012, p. 17, https://www.oecd.org/ctp/exchange-of-tax-information/keeping-it-safe-report.pdf, accessed 20 February 2017.

well as '[inadequate] resources and underdeveloped staff'.[33] This corresponds with the findings of the UN Tax Committee report, which states that revenue authorities in developing countries have identified a need for guidelines on the types of skills that are required to upscale the capacity of their international tax teams. As the TIE application matures it would therefore need to build in training on what the CbC reports tell you and how to use this information to conduct a risk assessment. This should be complemented by ongoing and rigorous training provided by development partners.

Capacity building needs to go beyond training of staff to include more innovations in ensuring the retention of such highly trained staff

However, capacity building needs to go beyond training of staff to include more innovations in ensuring the retention of such highly trained staff. The OECD report to the G20 DWG on the impact of BEPS in low-income countries shows that a persistent problem in many African revenue authorities is the retention of specialist skills. This is largely owing to less competitive salaries offered by revenue authorities, relative to the private sector.[34] Kenya has recognised this and overhauled its salary structures for its transfer pricing team to ensure that they are market-related and competitive. It has also invested in a strong leadership and team ethic, which creates a sense of stability for the transfer pricing team, thus leading to more effective staff retention. As a result of this successful intervention the IMF has declared the Kenyan Revenue Authority to be well equipped to handle the various complexities of transfer pricing.[35]

While bigger economies such as Kenya can afford to improve the remuneration packages of their staff, this is not always the case for many low-income countries in Africa. This poses a challenge to both the revenue authorities and the providers of international assistance, who fund the training of such specialists. If curbing transfer pricing is considered so critical to mobilising additional resources in African countries, then there may be a case for innovative solutions, such as development assistance being targeted to top up the salaries paid by revenue authorities to provide more remunerative packages.

33 ATAF, 'Transfer pricing (TP)', http://www.ataftax.org/en/TaxPrograms/Pages/TP.aspx, accessed 20 February 2017.

34 OECD, 13 August 2014b, *op. cit.*, p. 24.

35 *Ibid.*

How has CbCR been received in South Africa?

An interim report from the Davis Tax Committee, addressing base erosion and profit shifting in South Africa, proposed a much lower turnover threshold. It noted that 'it is recommended that preparing a Master file, Local file and country-by-country reporting should be compulsory for large Multinational businesses. A recommended threshold is businesses over ZAR[36] 1 billion (about $76,10 million) group turnover.'[37] This would ensure that relatively large MNEs are targeted and that multinational small and medium enterprises do not have to produce the same amount of documentation that might be expected from larger enterprises. The draft South African legislation,[38] on the other hand, recommends a threshold of ZAR 10 billion (which translates to the EUR 750 million as proposed by the OECD),[39] but this is likely to change given the recommendation from the Davis Tax Committee.

While the OECD has released an updated guideline on the implementation of CbCR on 12 October 2016[40] addressing the threshold issues in relation to currency fluctuations, the issues are only likely to be resolved during the 2020 review.[41]

All things considered, the South African government is prioritising the CbCR agenda, as expressed in initiatives such as the Davis Tax Committee, institutional configurations at the South African Revenue Service relating to the legislative amendments underway, and its active participation in global platforms that aim to foster coordination and possibly establish new standards vis-à-vis the promotion of transparency and disclosure. South Africa also has 13 bilateral TIEAs[42] currently in force, in addition to the entry into force of the Convention as amended by the Protocol, the publication of the Draft Regulations for purposes of paragraph (b) of the definition of 'international tax standard' in section 1, and related amendments to the Tax Administration Act of 2011. As soon as the CbC MCAA enters into force, South Africa will have the legislative framework to automatically exchange CbC reports with the other (currently 49) signatory states.

36 Currency code for the South African rand.

37 Davis Tax Committee, 'Addressing Base Erosion and Profit Shifting in South Africa: Davis Tax Committee Interim Report', 2015.

38 SARS (South African Revenue Service), 'Draft Regulations for Purposes of Paragraph (b) of the Definition of "International Tax Standard" in Section 1 of the Tax Administration Act, 2011', 2016, p. 3.

39 The regulations specify the CbCR standard for multinational enterprises.

40 OECD, 'Guidance on the Implementation of Country-by-Country Reporting – BEPS Action 13, OECD/G20 Base Erosion and Profit Shifting', 2016, http://www.oecd.org/tax/guidance-on-the-implementation-of-country-by-country-reporting-beps-action-13.pdf, accessed 4 December 2016.

41 This insight was secured during an interview with a South African government official.

42 With Argentina, Bahamas, Belize, Barbados, Bermuda, Cook Islands, Cayman Islands, Gibraltar, Guernsey, Jersey, Liberia, Liechtenstein and San Marino.

In general, developing countries do not face the same domestic political pressures as developed countries to implement the full BEPS agenda; nor do they possess the same institutional capacities as South Africa or other more advanced developing countries to assess its extent and develop tools to curb it. Consequently, the opportunity costs for African countries to prioritise the CbCR agenda are relatively higher.

Reaction to CbCR in the rest of the world

The cost of compliance has also been highlighted in the Davis Tax Committee's interim report, 'Action 13: Re-examine Transfer Pricing Documentation', as an international concern despite the transfer pricing documentation guidance provided by the OECD. From an MNE perspective, compliance with the reporting template represents a massive investment in terms of human resources and systems capability enhancements.[43] Other international concerns as identified in the Davis Tax Committee's interim report include confidentiality of taxpayer information, confidentiality of competitively sensitive data, concerns over the currencies in which information should be presented in the country-by-country template, and whether the taxes paid in each country should be reported on a cash or accrual basis.

On the other hand, states have also raised the question of whether publicly disclosing CbC reports might do more for tax transparency and address the capacity constraints in developing states, as MNEs and not the developing country tax authority would carry the compliance burden.

In the UK the All-Party Parliamentary Group (APPG) commends the work of the OECD in building international consensus on the development of new global tax rules and for making progress in gaining cross-country agreement on sharing tax information. However, the APPG mentions that[44]

> by failing to make the resulting data public the tax system is denied the transparency it requires. This would be particularly beneficial in developing countries where the revenue agencies may not have the capacity to ask for and use the relevant data they need to secure tax revenues from global companies.

The EU has called for public disclosure of CbCR, initially in the extractive and logging industries and credit institutions. More recently (12 April 2016)[45] the

43 Davis Tax Committee, *op. cit*.

44 APPG (All-Party Parliamentary Group), 'A more responsible global tax system or a "sticking plaster"?' August 2016, http://www.appgresponsibletax.org.uk/wp-content/uploads/2016/08/Sticking-Plaster-APPG-Responsible-Tax-Report.pdf, accessed 14 February 2017.

45 European Commission, 'Public country-by-country reporting / Corporate tax transparency', http://ec.europa.eu/finance/company-reporting/country-by-country-reporting/index_en.htm, accessed 25 August 2016.

European Commission adopted a proposal for a directive that imposes the publication of a yearly report on the profit and tax paid and other information on EU and non-EU multinational groups, the latter resident in the EU.

NGO's have also weighed in on public disclosure of CbCRs. In a joint civil society report, *Why Public Country-by-Country Reporting for Large Multinationals is a Must*,[46] the consortium notes that a lack of transparency makes aggressive tax planning difficult to quantify. The Q&A report notes that full public disclosure of CbCR will produce transparent data that is useful to assess the impact of governments' tax policies, provide a tool to increase governments' accountability, and re-establish public trust in MNEs and tax authorities.

While BEPS and CbCR focus on tax reporting to the tax authorities, many of the issues identified by global NGOs came after their reviewing the annual public financial statements of the relevant MNEs. Some MNEs such as Vodafone, Rio Tinto and SAB Miller responded to this challenge by preparing specific tax disclosure reports that are available publicly on their websites. The challenge is that there is no common approach or standard, which makes this information of less use than it could be. It is therefore important to understand whether the international reporting standards that govern the publication of an MNE's financial statements need to be reviewed as part of the tax disclosure discussion. In terms of commitment to international reporting standards, African states also lag behind the rest of the world. The International Financial Reporting Standards (IFRS), as developed by the International Accounting Standards Board, are the most widely adopted standards in the world. By implementing IFRS, countries can enhance the international comparability and quality of financial information, reduce the information gap and lower the costs of capital and international reporting by using a single, trusted, accounting language. Currently 143 jurisdictions use IFRS, but only 20 African states have adopted the standards, which contributes to the problem of comparability between countries' annual financial statements. This lag in standards adoption could further complicate the implementation of Action 13, as the distance to the proposed reporting standards could be much wider for some states that have not attempted to bridge the gap up to this point. It was noted during interviews with relevant government authorities in South Africa that only 14 African states have transfer pricing legislation in place, which contributes substantially to the lack of institutional capacity to implement Action 13 and productively use the information.

Full public disclosure of CbC reports will also address the limited capacity in some tax jurisdictions to fully assess MNEs' tax contributions. Based on our own consultations with stakeholders in South Africa, the cost of compliance for MNEs' full public disclosure of CbCR could be lower than expected, as large MNEs' tax directors are likely to have started a process to collect this data to disclose in their sustainability/integrated reports. Furthermore, public CbCR will cut down on the

46 Transparency International *et al.*, 'Why Public Country-by-Country Reporting for Large Multinationals is a Must: Questions and Answers', 24 February 2016, https://financialtransparency.org/wp-content/uploads/2016/02/Joint_Civil_Society_QA_pCBCR.pdf, accessed 19 August 2016.

time and cost of tax authorities to assess MNE tax compliance. According to the same NGO report, public disclosure of CbC reports is not likely to have a detrimental impact on large MNEs' competitiveness. For example, the subsidiary-by-subsidiary reporting requirement in India, demanding public disclosure of MNEs' revenues, pre-tax profits and tax on profits for all their subsidiaries, has not directly translated into a loss of competitiveness.[47]

Although some assistance is provided to low-capacity developing countries, the compliance burden still rests on revenue authorities' shoulders, whereas the public disclosure approach places the compliance burden on MNEs. Legislating public CbCR or public full tax disclosure could therefore free up revenue authority resources to conduct audits, and remove the need for such countries' revenue

Although some assistance is provided to low-capacity developing countries, the compliance burden still rests on revenue authorities' shoulders, whereas the public disclosure approach places the compliance burden on MNEs

authorities to comply with the technical requirements in the CbCR and EOI agreements. However, in the absence of EOI arrangements with the countries in which MNCs are headquartered, African countries would not be able to follow up on apparent anomalies. Furthermore, relations between group headquarters and subsidiaries in the jurisdiction in question follow several legal forms, with varying degrees of 'closeness' between the constituent organisations. For example, a group headquarters may only own a minority share in its African subsidiary, and therefore may not wish to share confidential group information with that subsidiary.

CONCLUSION: TOWARDS THE 2020 REVIEW

As it stands, CbCR has already achieved much in bringing attention to the need for cross-border tax authority cooperation. It has highlighted the basic requirements to conduct meaningful transfer pricing risk assessments and the need for a truly global approach to the problem. Nonetheless, the current state of the action plan is reflective of an agreement that has been carefully negotiated to have a wide appeal but that unfortunately had to make some, possibly substantial, concessions to achieve this. For this reason, a review of implementation, with a view to fine-tuning or even overhauling the system, was built in and will take place in 2020.

47 Transparency international, 'Transparency in Corporate Reporting: Assessing Emerging Market Multinationals', 2013, http://files.transparency.org/content/download/689/2960/file/2013_TRAC_EmergingMarketMultinationals_EN.pdf, accessed 27 August 2016.

Since the first CbC reports will only be due at the end of December 2017, it is currently too early to assess the effectiveness of the frameworks developed to govern the system. Nonetheless, from the analysis above, several issues are likely to feature in the 2020 review:

The threshold above which MNEs should be required to submit CbC reports

From our interviews it is apparent that African states favoured a much lower threshold – EUR 250 million ($850 million). By the time of the 2020 review, at least two years' worth of reports would have been generated, and other MNEs would be more aware of this process, and so it is possible that the idea of lowering the threshold would find a more receptive audience. Lowering the threshold is also likely to be beneficial to African states that meet the EOI requirements, since it would capture more MNEs in the risk assessment net.

The EOI requirements

Our interviewees, and some of the literature reviewed, point to these currently being too high for African states. However, given the trust barriers to lowering the requirements it is not clear that this issue could be resolved in favour of African states currently not able to comply.

The information contained in the CbCR template and associated Master file

It is premature to speculate on how the templates could be strengthened prior to implementation, but after implementation and subsequent scrutiny by many revenue authorities of the data generated and the templates governing it, the empirical basis will provide the grounds for a much more informed assessment of the strengths and limitations of CbCR.

Potential expansion of the scope of CIT to other taxes

Per the critique of CbCR briefly reviewed above, the application of CbCR to other taxes paid by MNEs could also be considered.

Transparency of CbC reports

Again, the civil society critique has highlighted a need for greater transparency in the publication of CbC reports, with a view to full public disclosure. This will, no doubt, feature in the review and African revenue authorities will need to engage with the issues.

APPENDIX

TABLE 3 OVERVIEW OF ALLOCATION OF INCOME, TAXES AND BUSINESS ACTIVITIES BY TAX JURISDICTION

NAME OF THE MNE GROUP:		
FISCAL YEAR CONCERNED:		
CURRENCY USED:		
Tax jurisdiction		
Revenues	Unrelated party[h]	
	Related party[i]	
	Total	
Profit (loss) before income tax[a]		
Income tax paid (on cash basis)[b]		
Income tax accrued – current year[c]		
Stated capital[d]		
Accumulated earnings[e]		
Number of employees[f]		
Tangible assets other than cash and cash equivalents[g]		

a The profit (loss) before income tax should include all extraordinary income and expense items.

b The total amount of income tax actually paid during the relevant fiscal year by all the constituent entities resident for tax purposes in the relevant tax jurisdiction.

c The sum of the accrued current tax expense recorded on taxable profits or losses of the year of reporting of all the constituent entities resident for tax purposes in the relevant tax jurisdiction.

d The sum of the stated capital of all the constituent entities resident for tax purposes in the relevant tax jurisdiction.

e The sum of the total accumulated earnings of all the constituent entities resident for tax purposes in the relevant tax jurisdiction as of the end of the year.

f The total number of employees on a full-time equivalent (FTE) basis of all the Constituent Entities resident for tax purposes in the relevant tax jurisdiction.

g The sum of the net book values of tangible assets of all the constituent entities resident for tax purposes in the relevant tax jurisdiction.

h The sum of revenues of all the constituent entities of the MNE group in the relevant tax jurisdiction generated from transactions with independent parties.

i The sum of revenues of all the constituent entities of the MNE group in the relevant tax jurisdiction generated from transactions with associated enterprises.

Source: OECD, 'Transfer Pricing Documentation and Country-By-Country Reporting, Action 13 – 2015 Final Report', 2015

TABLE 4 LIST OF ALL THE CONSTITUENT ENTITIES OF THE MNE GROUP INCLUDED IN EACH AGGREGATION PER TAX JURISDICTION

NAME OF THE MNE GROUP:

FISCAL YEAR CONCERNED:

Tax jurisdiction				
		1	2	3
Constituent entities resident in the tax jurisdiction				
Tax jurisdiction of organisation or incorporation if different from tax jurisdiction of residence				
Main business activity(ies)	Research and development			
	Holding or managing			
	Intellectual property			
	Purchasing or procurement			
	Manufacturing or production			
	Sales, marketing or distribution			
	Administrative, management or support services			
	Provision of services to unrelated parties			
	Internal group finance			
	Regulated financial services			
	Insurance			
	Holding shares or other equity instruments			
	Dormant			
	Other			

Source: OECD, *op. cit.*

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