

OECD releases progress report on preferential regimes under BEPS Action 5

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Executive Summary

On 16 October 2017, the Organisation for Economic Co-operation and Development (OECD) released *Harmful Tax Practices - 2017 Progress Report on Preferential Regimes* (the Progress Report), approved by the Inclusive Framework on Base Erosion and Profit Shifting (BEPS). The purpose of this document is to provide an update to the 2015 BEPS Action 5 report and to report the results of the review of all Inclusive Framework members' preferential tax regimes that have been identified.

To assist and support the consistent and swift implementation of BEPS Action 5, the Progress Report also contains guidance on preferential tax regimes, timelines for amending regimes and recommendations on monitoring certain features of preferential regimes.

Detailed discussion

Background

Recognizing the need to realign taxation of profits with the substantial activities that generate them and to improve transparency, the OECD started work on addressing harmful tax competition in the late 1990s, resulting in a 1998 report, *Harmful Tax Competition: An Emerging Global Issue*. Under this

initiative, the OECD also created the Forum on Harmful Tax Practices (FHTP) to take the work forward. Following its creation, the FHTP has been the body with the mandate to monitor and review tax practices of jurisdictions around the world, focusing on the features of preferential tax regimes.

On 5 October 2015, the OECD released its final report on Action 5, *Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance* (the Action 5 Report) under its BEPS Action Plan.¹ The Action 5 Report covers two main areas: (i) the definition of a “substantial activity” criterion to be applied when determining whether tax regimes are harmful; and (ii) improving transparency.

The Action 5 Report is one of the four BEPS minimum standards. Each of the four BEPS minimum standards is subject to peer review in order to ensure timely and accurate implementation and thus safeguard the level playing field. All members of the Inclusive Framework on BEPS commit to implementing the Action 5 minimum standard, and commit to participating in the peer review. To that end, on 1 February 2017, the OECD released the *Terms of Reference and Methodology for Peer Reviews* on the Action 5 standard for the exchange of information on tax rulings.²

The Progress Report

After the publication of the Action 5 Report, the FHTP has reviewed compliance of 164 preferential regimes with the BEPS Action 5 minimum standard. The Progress Report includes the results of the review of these regimes that have been agreed by the FHTP over the course of five meetings, held between November 2016 and September 2017, and it reflects results as of October 2017.

The regimes have generally been reviewed using a thematic approach, whereby regimes of a similar nature are reviewed together. The FHTP has split the regimes into nine broad categories: (1) IP regimes, (2) headquarters regimes, (3) financing and leasing regimes, (4) banking and insurance regimes, (5) distribution and service center regimes, (6) shipping regimes, (7) holding company regimes, (8) fund management regimes, and (9) miscellaneous regimes.

The review process involves each jurisdiction which offers a relevant regime completing a standardized self-review questionnaire and submitting the relevant legislation to the FHTP. The next step is a discussion of each regime at the periodic meetings of delegates of the FHTP, which includes a dialogue with the jurisdiction in order to provide any clarifying

information. Decisions are reached on a consensus basis, and where necessary on a “consensus minus one” basis of decision making in relation to the peer review process.

The Progress Report contains tables with the reviewed regimes, each of them being characterized as (i) “harmful” when the regime has harmful features and economic effects; (ii) “potentially harmful” when the features of the regime implicate one or more of the criteria, but an assessment of the economic effects has not yet taken place to make a determination as to whether the regime is “harmful”; (iii) “abolished” when the regime is in the process of being eliminated because no new entrants are permitted into the regime, a definite date for complete abolition of the regime has been announced, and the regime is transparent and has effective exchange of information; (iv) “amended” when the regime has had its harmful features removed and is therefore not harmful anymore; and (v) “in the process of being eliminated” or “in the process of being amended” when the jurisdiction has communicated to the FHTP its government’s commitment to abolish or amend the regime in light of the discussions by the FHTP about the features of the regime that are of concern, and the FHTP could reconsider the description of these regimes if insufficient progress was being made.

Finally, the Progress Report includes four annexes with guidance and recommendations. These annexes refer to: (i) timelines for implementing the nexus approach for IP regimes; (ii) guidance on the closing off of regimes and grandfathering for non-IP regimes; (iii) monitoring data on preferential regimes; and (iv) substantial activities in non-IP regimes.

Implications

The Progress Report demonstrates the swift progress being made in the implementation of BEPS Action 5 and it affirms the actions of Inclusive Framework members that have made significant commitments to change their tax rules. The release of this report also provides clarity to taxpayers on the status of preferential regimes in jurisdictions in which they operate. The FHTP will continue its work, including the monitoring and review of preferential tax regimes which are being amended to conform to the Action 5 standard.

Taxpayers should monitor the work of the FHTP on the regimes that are found to be harmful and are in the process of being amended or eliminated.

Endnotes

1. See EY Global Tax Alert, [OECD releases final report on countering harmful tax practices under Action 5](#), dated 8 October 2015.
2. See EY Global Tax Alert, [OECD releases peer review documents on BEPS Action 5 on Harmful Tax Practices and on BEPS Action 13 on Country-by-Country Reporting](#), dated 6 February 2017.

For additional information with respect to this Alert, please contact the following:

Ernst & Young Belastingadviseurs LLP, Rotterdam

- ▶ Ronald van den Brekel ronald.van.den.brekel@nl.ey.com
- ▶ Marlies de Ruiter marlies.de.ruiter@nl.ey.com

Ernst & Young LLP, Global Tax Desk Network, New York

- ▶ Gerrit Groen gerrit.groen@ey.com
- ▶ Jose A. (Jano) Bustos joseantonio.bustos@ey.com
- ▶ David Corredor-Velásquez david.corredorvelasquez@ey.com

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EYG no. 05891-171Gbl

1508-1600216 NY
ED None

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